



# Anglian Water Services Financing Plc

(incorporated with limited liability in England and Wales with registered number 4330322)

**€10,000,000,000 Global Secured Medium Term Note Programme**

unconditionally and irrevocably guaranteed by, inter alios,

**Anglian Water Services Limited**

(incorporated with limited liability in England and Wales with registered number 2366656)



Anglian Water Services Financing Plc  
and Anglian Water Services Ltd  
are part of the AWG group

**BARCLAYS**

**anglianwater**

**ANGLIAN WATER SERVICES FINANCING PLC**  
(incorporated with limited liability in England and Wales with registered number 4330322)

€10,000,000,000

**Global Secured Medium Term Note Programme**  
**unconditionally and irrevocably guaranteed by, *inter alios*,**  
**ANGLIAN WATER SERVICES LIMITED**  
(incorporated with limited liability in England and Wales with registered number 2366656)

**for the issuance of**  
**Guaranteed Unwrapped Bonds**

On 23 July 2002, the Issuer (as defined below) entered into a €10,000,000,000 Global Secured Medium Term Note Programme (the “**Programme**”). The Programme was updated on 28 July 2004. This document supersedes the Offering Circular dated 23 July 2002, the Offering Circular dated 24 June 2003 and the Offering Circular dated 28 July 2004. Under the Programme, Anglian Water Services Financing Plc (the “**Issuer**”) may from time to time, on or after the date of this Prospectus, issue bonds (the “**Bonds**”), subject to the provisions described herein, in bearer or registered form (respectively “**Bearer Bonds**” and “**Registered Bonds**”). This Prospectus does not affect any Bonds issued before the date of this Prospectus.

The payment of all amounts owing in respect of the Bonds will be unconditionally and irrevocably guaranteed by Anglian Water Services Limited (“**Anglian Water**” or “**AWS**”), Anglian Water Services Holdings Limited (“**Anglian Water Services Holdings Ltd**” or “**AWS Holdings**”) and Anglian Water Services Overseas Holdings Limited (“**Anglian Water Services Overseas Holdings Ltd**” or “**AWS Overseas Holdings**”) as described herein. Anglian Water, the Issuer, Anglian Water Services Holdings Ltd and Anglian Water Services Overseas Holdings Ltd are together referred to herein as the “**Obligors**”. Anglian Water Services Holdings Ltd was incorporated in England and Wales under the Companies Act 1985 (as amended) as a limited company on 28 November 2001, whilst Anglian Water Services Overseas Holdings Ltd was incorporated in the Cayman Islands on 16 January 2002 as an exempted company with limited liability. Anglian Water Services Holdings Ltd and Anglian Water Services Overseas Holdings Ltd do not have any significant assets other than the shares in their respective subsidiaries.

Subject to (i) the approval of the Dealers (and confirmation of no downgrade of the Bonds in issue which benefit from a financial guarantee insurance policy (the “**Wrapped Bonds**”) from at least two of the Rating Agencies (as defined below)) and (ii) the publication of a supplemental prospectus or a new prospectus, the Issuer may arrange for any financial institution to issue bond policies (“**Bond Policies**”) in respect of new Series of Class A Wrapped Bonds and/or Class B Wrapped Bonds (such financial institution, a “**Financial Guarantor**”). The other Bonds issued or to be issued under the Programme (the “**Unwrapped Bonds**”) do not, or in respect of Bonds to be issued under the Programme, will not benefit from a financial guarantee insurance policy of any financial institution. For the avoidance of doubt, the Issuer may not as of the date of this Prospectus issue Wrapped Bonds pursuant to this Prospectus.

The maximum aggregate nominal amount of all Bonds from time to time outstanding under the Programme will not exceed €10,000,000,000 (or its equivalent in other currencies calculated as described herein), subject to increase as described herein.

Bonds issued under the Programme will be issued in series (each a “**Series**”), with each Series belonging to one of four classes (each a “**Class**”). The Wrapped Bonds will be designated as either “**Class A Wrapped Bonds**” or “**Class B Wrapped Bonds**”. The Unwrapped Bonds will be designated as either “**Class A Unwrapped Bonds**” or “**Class B Unwrapped Bonds**”. Each Series will comprise one or more Tranches (each a “**Tranche**”) of Bonds which are identical in all respects save for the issue dates, interest commencement dates and/or issue prices, and which are expressed to be consolidated and form a single Series.

The Bonds may be issued on a continuing basis to one or more of the Dealers specified under Chapter 1, “**Parties**” and any additional Dealer appointed under the Programme from time to time by the Issuer (each a “**Dealer**” and together the “**Dealers**”), which appointment may be for a specific issue or on an ongoing basis. References in this Prospectus to the “**relevant Dealer**” shall, in the case of an issue of Bonds being (or intended to be) subscribed by more than one Dealer, be to all Dealers agreeing to subscribe such Bonds.

Application has been made to the Financial Services Authority in its capacity as competent authority under the Financial Services and Markets Act 2000 (the “**UK Listing Authority**”) for Bonds issued under the Programme for the period of 12 months from the date of this Prospectus to be admitted to the official list of the UK Listing Authority (the “**Official List**”) and to the London Stock Exchange plc (the “**London Stock Exchange**”) for such Bonds to be admitted to trading on the London Stock Exchange’s Gilt Edged and Fixed Interest Market (the “**Market**”). References in this Prospectus to Bonds being “**listed**” (and all related references) shall mean that such Bonds have been admitted to trading on the Market and have been admitted to the Official List. The Market is a regulated market for the purposes of the Investment Services Directive 93/22/EC.

In respect of Bonds to be issued under the Programme, notice of the aggregate nominal amount of Bonds, interest (if any) payable in respect of Bonds, the issue price of Bonds and any other terms and conditions not contained herein which are applicable to each Tranche of Bonds will be set out in a set of final terms (the “**Final Terms**”) which, with respect to Bonds to be admitted to the Official List and admitted on the Market, will be delivered to the UK Listing Authority and the London Stock Exchange on or before the date of issue of the Bonds of such Tranche.

The Programme provides that Bonds may be listed on such other or further stock exchange(s) as may be agreed between the Obligors and the relevant Dealer. The Issuer may also issue unlisted Bonds.

**Prospective investors should have regard to the factors described under Chapter 6 headed “Risk Factors” in this Prospectus.**

The Bonds and the guarantees in respect thereof have not been and will not be registered under the U.S. Securities Act of 1933, as amended (the “**Securities Act**”) or with any securities regulatory authority of any State or other jurisdiction of the United States, and the Bonds may include Bearer Bonds that are subject to U.S. tax law requirements. Subject to certain exceptions, the Bonds may not be offered or sold or, in the case of Bearer Bonds, delivered within the United States or to, or for the account or benefit of, U.S. persons (as defined in Regulation S under the Securities Act (“**Regulation S**”) in the case of Registered Bonds, or as defined in the U.S. Internal Revenue Code of 1986, as amended, and regulations thereunder in the case of Bearer Bonds). See Chapter 8, “**Form of the Bonds**” for a description of the manner in which Bonds will be issued. Registered Bonds are subject to certain restrictions on transfer. See Chapter 15, “**Subscription and Sale and Transfer and Selling Restrictions**”.

Each Tranche of Class A Wrapped Bonds, Class A Unwrapped Bonds and Class B Unwrapped Bonds is expected on issue to have the following credit ratings from the respective credit rating agencies below. The credit ratings will be specified in the relevant Final Terms.

<i>Class</i>	<i>Standard &amp; Poor’s</i>	<i>Moody’s</i>	<i>Fitch</i>
Class A Wrapped Bonds .....	AAA	Aaa	AAA
Class A Unwrapped Bonds .....	A-	A3	A-
Class B Unwrapped Bonds .....	BBB	Baa3	BBB

Any ratings ascribed to the Bonds reflect only the views of Moody’s Investors Service Limited (“**Moody’s**”), Standard & Poor’s Ratings Services, a Division of the McGraw Hill Companies Inc. (“**Standard & Poor’s**” or “**S&P**”) and Fitch Ratings Ltd (“**Fitch**”) and, together with Moody’s and Standard & Poor’s, the “**Rating Agencies**”). A rating is not a recommendation to buy, sell or hold securities and may be subject to suspension, change or withdrawal at any time by the assigning rating agency.

In the case of any Bonds which are to be admitted to trading on a regulated market within the European Economic Area or offered to the public in a Member State of the European Economic Area in circumstances which require the publication of a prospectus under the Prospectus Directive (2003/71/EC), the minimum denomination shall be €50,000 (or its equivalent in any other currency as at the date of issue of the Bonds).

The Obligors may agree with any Dealer and Deutsche Trustee Company Limited (the “**Bond Trustee**”) that Bonds may be issued in a form not contemplated by the Terms and Conditions of the Bonds herein, in which event (in the case of Bonds admitted to the Official List only) a supplementary prospectus, if appropriate, will be made available which will describe the effect of the agreement reached in relation to such Bonds.

Arranger  
**Barclays Capital**  
Dealers

**Barclays Capital**  
**Citigroup**  
**Dresdner Kleinwort Wasserstein**  
**HVB Corporates & Markets**  
**The Royal Bank of Scotland**

**BNP PARIBAS**  
**Deutsche Bank**  
**HSBC**  
**ING Wholesale Banking**  
**JPMorgan**

## IMPORTANT NOTICE

This Prospectus comprises a base prospectus for the purposes of Article 5.4 of Directive 2003/71/EC (the “Prospectus Directive”) and for the purpose of giving information with regard to the Issuer and the other Obligors which, according to the particular nature of the Issuer and the Bonds, is necessary to enable investors to make an informed assessment of the assets and liabilities, financial position, profit and losses and prospects of the Issuer.

Each of the Issuer and the other Obligors accepts responsibility for the information contained in or appended to this Prospectus. To the best of the knowledge of each of the Issuer and the other Obligors (each having taken all reasonable care to ensure that such is the case), the information contained in this Prospectus is in accordance with the facts and does not omit anything likely to affect the import of such information.

This Prospectus is being distributed only to, and is directed only at persons who are (i) outside the United Kingdom or (ii) are persons who have professional experience in matters relating to investments falling within Article 19(1) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001 (the “Order”) or (iii) are high net worth entities, and other persons to whom it may lawfully be communicated, falling within Article 49(1) of the Order (all such persons together being referred to as “relevant persons”). This Prospectus, or any of its contents, must not be acted on or relied on by persons who are not relevant persons. Any investment or investment activity to which this Prospectus relates is available only to, and any invitation, offer or agreement to subscribe, purchase or otherwise acquire such investments will be engaged in only, with relevant persons.

Copies of each set of Final Terms (in the case of Bonds to be admitted to the Official List) will be available from FT Business Research Centre, operated by FT Electronic Publishing at Fitzroy House, 13-15 Epworth Street, London EC2A 4DL and from the specified office set out below of each of the Paying Agents (as defined below).

This Prospectus is to be read in conjunction with all documents which are deemed to be incorporated herein by reference (see “*Documents Incorporated by Reference*” below).

The Series of Wrapped Bonds issued on 30 July 2002 have the benefit of financial guarantee insurance policies, issued by MBIA Assurance S.A. (“MBIA”). For any further Series of Wrapped Bonds issued, a new financial guarantee insurance policy will be entered into and dated as of the issue date of such Series of Wrapped Bonds, by MBIA or another Financial Guarantor in respect of such Bonds and a supplemental prospectus or a new prospectus will be published as described above.

None of the Dealers, the Bond Trustee, the Security Trustee, the Hedge Counterparties, the Finance Lessors, the Authorised Credit Providers, the Debt Service Reserve Liquidity Facility Provider, the O&M Reserve Facility Provider, the Original Lenders and the Agents or any Facility Agent (each as defined herein and together, the “Other Parties”) has independently verified the information contained herein. Accordingly, no representation, warranty or undertaking, express or implied, is made and no responsibility or liability is accepted by the Dealers, the Bond Trustee, the Security Trustee or the Other Parties as to the accuracy or completeness of the information contained or incorporated in this Prospectus or any other information provided by the Obligors in connection with the Programme. None of the Dealers, the Bond Trustee, the Security Trustee or the Other Parties accepts any liability in relation to the information contained or incorporated by reference in this Prospectus or any other information provided by the Obligors in connection with the Programme.

No person is or has been authorised by any of the Obligors, any of the Dealers, the Bond Trustee, the Security Trustee or the Other Parties to give any information or to make any representation not contained in or not consistent with this Prospectus or any other information supplied in connection with the Programme or the Bonds and, if given or made, such information or representation must not be relied upon as having been authorised by any of the Obligors, any of the Dealers, the Bond Trustee, the Security Trustee or the Other Parties.

Neither this Prospectus nor any other information supplied in connection with the Programme or any Bonds (i) is intended to provide the basis of any credit or other evaluation or (ii) should be considered as a recommendation by the Obligors, the Bond Trustee, the Security Trustee, any of the Dealers or the Other Parties that any recipient of this Prospectus or any other information supplied in connection with

the Programme or any Bonds should purchase any Bonds. Each investor contemplating purchasing any Bonds should make its own independent investigation of the financial condition and affairs, and its own appraisal of the creditworthiness, of the Obligors. Neither this Prospectus nor any other information supplied in connection with the Programme or the issue of any Bonds constitutes an offer or invitation by or on behalf of any of the Obligors, any of the Dealers, the Bond Trustee, the Security Trustee or the Other Parties to any person to subscribe for or to purchase any Bonds.

Neither the delivery of this Prospectus nor the offering, sale or delivery of any Bonds shall in any circumstances imply that the information contained herein concerning the Obligors is correct at any time subsequent to the date hereof or that any other information supplied in connection with the Programme is correct or that there has been no adverse change in the financial position of the Issuer as of any time subsequent to the date indicated in the document containing the same. Neither the Dealers, the Bond Trustee, the Security Trustee or the Other Parties expressly undertake to review the financial condition or affairs of any of the Obligors during the life of the Programme or to advise any investor in the Bonds of any information coming to their attention. Investors should review the most recently published documents incorporated by reference into this Prospectus when deciding whether or not to purchase any Bonds.

This Prospectus does not constitute an offer to sell or the solicitation of an offer to buy any Bonds in any jurisdiction to any person to whom it is unlawful to make the offer or solicitation in such jurisdiction. The distribution of this Prospectus and the offer or sale of Bonds may be restricted by law in certain jurisdictions. None of the Obligors, the Dealers, the Bond Trustee, the Security Trustee or the Other Parties represents that this Prospectus may be lawfully distributed, or that any Bonds may be lawfully offered, in compliance with any applicable registration or other requirements in any such jurisdiction, or pursuant to an exemption available thereunder, or assumes any responsibility for facilitating any such distribution or offering. In particular, no action has been taken by the Obligors, the Dealers, the Bond Trustee, the Security Trustee or the Other Parties which would permit a public offering of any Bonds or distribution of this Prospectus in any jurisdiction where action for that purpose is required. Accordingly, no Bonds may be offered or sold, directly or indirectly, and neither this Prospectus nor any advertisement or other offering material may be distributed or published in any jurisdiction, except under circumstances that will result in compliance with any applicable laws and regulations. Persons into whose possession this Prospectus or any Bonds may come must inform themselves about, and observe, any such restrictions on the distribution of this Prospectus and the offering and sale of Bonds. In particular, there are restrictions on the distribution of this Prospectus and the offer or sale of Bonds in the United States, the United Kingdom, the Cayman Islands, Japan, Germany and The Netherlands. See Chapter 15, "*Subscription and Sale and Transfer and Selling Restrictions*".

In making an investment decision, investors must rely on their own examination of the Obligors and the terms of the Bonds being offered, including the merits and risks involved. The Bonds and the guarantees in respect thereof have not been approved or disapproved by the United States Securities and Exchange Commission, any State securities commission or any other regulatory authority in the United States, nor have the foregoing authorities approved this Prospectus or confirmed the accuracy or determined the adequacy of the information contained in this Prospectus. Any representation to the contrary is a criminal offence in the United States.

None of the Dealers, the Obligors, the Bond Trustee, the Security Trustee or the Other Parties makes any representation to any investor in the Bonds regarding the legality of its investment under any applicable laws. Any investor in the Bonds should be able to bear the economic risk of an investment in the Bonds for an indefinite period of time.

## U.S. INFORMATION

This Prospectus is being distributed on a confidential basis in the United States to a limited number of QIBs or Institutional Accredited Investors (each as defined under Chapter 8, “*Form of the Bonds*”) for informational use solely in connection with the consideration of the purchase of the Bonds being offered hereby. Its use for any other purpose in the United States is not authorised. It may not be copied or reproduced in whole or in part nor may it be distributed or any of its contents disclosed to anyone other than the prospective investors to whom it is originally submitted.

Registered Bonds may be offered or sold within the United States only to QIBs or to Institutional Accredited Investors, in either case in transactions exempt from registration under the Securities Act. Each U.S. purchaser of Registered Bonds is hereby notified that the offer and sale of any Registered Bonds to it may be made in reliance upon the exemption from the registration requirements of the Securities Act provided by Rule 144A under the Securities Act (“Rule 144A”).

Purchasers of Definitive IAI Registered Bonds will be required to execute and deliver an IAI Investment Letter (as defined under Chapter 9, “*Terms and Conditions of the Bonds*”). Each purchaser or holder of Definitive IAI Registered Bonds, Bonds represented by a Rule 144A Global Bond or any Bonds issued in registered form in exchange or substitution therefor (together “Legended Bonds”) will be deemed, by its acceptance or purchase of any such Legended Bonds, to have made certain representations and agreements intended to restrict the resale or other transfer of such Legended Bonds as set out in Chapter 15, “*Subscription and Sale and Transfer and Selling Restrictions*”. Unless otherwise stated, terms used in this paragraph have the meanings given to them in “*Form of the Bonds*”.

## NOTICE TO NEW HAMPSHIRE RESIDENTS

NEITHER THE FACT THAT A REGISTRATION STATEMENT OR AN APPLICATION FOR A LICENCE HAS BEEN FILED UNDER CHAPTER 421-B OF THE NEW HAMPSHIRE REVISED STATUTES WITH THE STATE OF NEW HAMPSHIRE NOR THE FACT THAT A SECURITY IS EFFECTIVELY REGISTERED OR A PERSON IS LICENSED IN THE STATE OF NEW HAMPSHIRE CONSTITUTES A FINDING BY THE SECRETARY OF STATE OF NEW HAMPSHIRE THAT ANY DOCUMENT FILED UNDER RSA 421-B IS TRUE, COMPLETE AND NOT MISLEADING. NEITHER ANY SUCH FACT NOR THE FACT THAT AN EXEMPTION OR EXCEPTION IS AVAILABLE FOR A SECURITY OR A TRANSACTION MEANS THAT THE SECRETARY OF STATE HAS PASSED IN ANY WAY UPON THE MERITS OR QUALIFICATIONS OF, OR RECOMMENDED OR GIVEN APPROVAL TO, ANY PERSON, SECURITY OR TRANSACTION. IT IS UNLAWFUL TO MAKE, OR CAUSE TO BE MADE, TO ANY PROSPECTIVE PURCHASER, CUSTOMER OR CLIENT ANY REPRESENTATION INCONSISTENT WITH THE PROVISIONS OF THIS PARAGRAPH.

## AVAILABLE INFORMATION

To permit compliance with Rule 144A in connection with any resales or other transfers of Bonds that are “restricted securities” within the meaning of the Securities Act, the Issuer and each of the other Obligors has undertaken to furnish, upon the request of a holder of such Bonds or any beneficial interest therein, to such holder or to a prospective purchaser designated by him, the information required to be delivered under Rule 144A(d)(4) under the Securities Act if, at the time of the request, the Issuer is neither a reporting company under Section 13 or 15(d) of the U.S. Securities Exchange Act of 1934, as amended (the “Exchange Act”), nor exempt from reporting pursuant to Rule 12g3-2(b) thereunder.

## CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Prospectus includes “forward-looking statements” within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act. All statements other than statements of historical facts included in this Prospectus, including, without limitation, those regarding Anglian Water’s financial position, business strategy, plans and objectives of management for future operations (including development plans and objectives relating to Anglian Water’s services), are forward-looking statements.

Such forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of Anglian Water, or industry results, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such forward-looking statements are based on numerous assumptions regarding Anglian Water's present and future business strategies and the environment in which Anglian Water will operate in the future. The important factors that could cause Anglian Water's actual results, performance or achievements to differ materially from those in the forward-looking statements include, among others, legislative, regulatory or other circumstances affecting anticipated revenues, costs or capital expenditure requirements, future climatic and environmental conditions, future economic conditions including changes in customer demand, development of competition within the water supply and sewerage industry and changes in capital market conditions. Additional factors that could cause actual results, performance or achievements to differ materially include, but are not limited to, those discussed under Chapter 6, "Risk Factors". These forward-looking statements speak only as of the date of this Prospectus. Anglian Water expressly disclaims any obligation or undertaking to release publicly any updates or revisions to any forward-looking statement contained herein to reflect any change in Anglian Water's expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based.

#### **SERVICE OF PROCESS AND ENFORCEMENT OF CIVIL LIABILITIES**

Each of the Issuer, Anglian Water and Anglian Water Services Holdings Ltd is a corporation organised under the laws of England and Wales. All of the officers and directors of the Issuer, Anglian Water and Anglian Water Services Holdings Ltd named herein reside outside the United States and all or a substantial portion of the assets of the Issuer, Anglian Water and Anglian Water Services Holdings Ltd and of such officers and directors are located outside the United States. As a result, it may not be possible for investors to effect service of process outside England upon the Issuer, Anglian Water or Anglian Water Services Holdings Ltd, as the case may be, or such persons, or to enforce judgments against them obtained in courts outside England predicated upon civil liabilities of the Issuer, Anglian Water or Anglian Water Services Holdings Ltd, as the case may be, or such directors and officers under laws other than English law, including any judgment predicated upon United States federal securities laws or securities laws of any State or territory within the United States.

Each of the Issuer, Anglian Water and Anglian Water Services Holdings Ltd has been advised by Linklaters, its counsel, that there is doubt as to the enforceability in England in original actions or in actions for enforcement of judgments of United States courts of civil liabilities predicated solely upon the federal securities laws of the United States.

Anglian Water Services Overseas Holdings Ltd is a corporation organised under the laws of the Cayman Islands. All of the officers and directors of Anglian Water Services Overseas Holdings Ltd named herein reside outside the United States and all or a substantial portion of the assets of Anglian Water Services Overseas Holdings Ltd and of such officers and directors are located outside the United States. As a result, it may not be possible for investors to effect service of process outside the Cayman Islands upon Anglian Water Services Overseas Holdings Ltd or such persons, or to enforce judgments against them obtained in courts outside the Cayman Islands predicated upon civil liabilities of Anglian Water Services Overseas Holdings Ltd or such directors and officers under laws other than Cayman Islands law, including any judgment predicated upon United States federal securities laws or securities laws of any State or territory within the United States.

Anglian Water Services Overseas Holdings Ltd has been advised by Maples and Calder Europe, its counsel, that there is doubt as to the enforceability in the Cayman Islands in original actions or in actions for enforcement of judgments of United States courts of civil liabilities predicated solely upon the federal securities laws of the United States.

## PRESENTATION OF FINANCIAL AND OTHER INFORMATION

Each of the Issuer, Anglian Water, Anglian Water Services Holdings Ltd and Anglian Water Services Overseas Holdings Ltd maintains its financial books and records and prepares its financial statements in Sterling in accordance with generally accepted accounting principles in the United Kingdom (“U.K. GAAP”) which differ in certain significant respects from generally accepted accounting principles in the United States (“U.S. GAAP”). See Chapter 17, “*Summary of Certain Significant Differences between U.K. GAAP and U.S. GAAP*”.

All references in this Prospectus to “Sterling” and “£” refer to pounds sterling, to “U.S. dollars”, “U.S.\$” and “\$” refer to United States dollars and to “euro” and “€” refer to the currency introduced at the start of the third stage of European economic and monetary union pursuant to the Treaty establishing the European Community, as amended.

## STABILISATION

In connection with the issue and distribution of any Tranche of Bonds, the Dealer (if any) disclosed as the stabilising manager in the applicable Final Terms or any person acting for him may over-allot (provided that, in the case of any Tranche of Bonds to be admitted to trading on the Market, the aggregate principal amount of Bonds allotted does not exceed 105 per cent. of the aggregate principal amount of the relevant Tranche) or effect transactions with a view to supporting the market price of the Bonds of the Series (as defined below) of which such Tranche forms part at a level higher than that which might otherwise prevail. However, there is no assurance that the stabilising manager or any agent of his will undertake stabilisation action. Any stabilisation action may begin on or after the date on which adequate public disclosure of the terms of the offer of the relevant Tranche of Bonds is made and, if begun, may be ended at any time, but it must end no later than the earlier of 30 days after the Issue Date of the relevant Tranche of Bonds and 60 days after the date of the allotment of the relevant Tranche of Bonds.

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## DOCUMENTS INCORPORATED BY REFERENCE

This Prospectus should be read and construed in conjunction with the audited consolidated annual financial statements and audited non-consolidated financial statements of each of the Obligors for the financial years ended 31 March 2004 and 2005 together in each case with the audit report thereon, which have been previously published or are published simultaneously with this Prospectus and which have been approved by the Financial Services Authority or filed with it (respectively in relation to each Obligor, the “**2004 Annual Report**” and the “**2005 Annual Report**” and see Chapter 16, “*General Information*” for a description of the financial statements currently published by each of the Obligors) save that any statement contained herein or in a document which is deemed to be incorporated by reference herein shall be deemed to be modified or superseded for the purpose of this Prospectus to the extent that a statement contained in any such subsequent document which is deemed to be incorporated by reference herein modifies or supersedes such earlier statement (whether expressly, by implication or otherwise). Any statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this Prospectus.

Each Obligor will provide, without charge, to each person to whom a copy of this Prospectus has been delivered, upon the request of such person, a copy of any or all of the documents deemed to be incorporated herein by reference unless such documents have been modified or superseded as specified above. Requests for such documents should be directed to any of the Obligors at their respective offices set out at the end of this Prospectus.

Each of the Obligors has undertaken to the Dealers in the Programme Agreement (as defined in Chapter 15, “*Subscription and Sale and Transfer and Selling Restrictions*”) to comply with Section 81 of the Financial Services and Markets Act 2000.

If the terms of the Programme are modified or amended in a manner which would make this Prospectus, as so modified or amended, inaccurate or misleading, a new prospectus will be prepared.

## SUPPLEMENTARY PROSPECTUS

The Issuer has undertaken, in connection with the admission of the Bonds to the Official List and to trading on the Market, that, if there shall occur any significant new factor, mistake or material inaccuracy relating to information contained in this Prospectus which is capable of affecting the assessment of any Bonds whose inclusion would reasonably be required by investors and their professional advisers, and would reasonably be expected by them to be found in this Prospectus, for the purpose of making an informed assessment of the assets and liabilities, financial position, profits and losses and prospects of the relevant Issuer, and the rights attaching to the Bonds, the Issuer shall prepare a supplement to this Prospectus or publish a replacement prospectus for use in connection with any subsequent issue by the Issuer of Bonds and will supply to each Dealer and the Bond Trustee such number of copies of such supplement hereto or replacement prospectus as such Dealer and Bond Trustee may reasonably request. The Issuer will also supply to the UK Listing Authority such number of copies of such supplement hereto or replacement prospectus as may be required by the UK Listing Authority and will make copies available, free of charge, upon oral or written request, at the specified offices of the Paying Agents (as defined herein).

If at any time any Issuer shall be required to prepare a supplemental prospectus pursuant to Section 87(G) of the Financial Services and Markets Act 2000 (the “FSMA”), the Issuer shall prepare and make available an appropriate supplement to this Prospectus or a further prospectus which, in respect of any subsequent issue of Bonds to be listed on the Official List and admitted to trading on the Market, shall constitute a supplemental prospectus as required by the UK Listing Authority and Section 87(G) of the FSMA.

## GENERAL DESCRIPTION OF THE PROGRAMME

Under the Programme, the Issuer may from time to time issue Bonds denominated in any currency, subject as set out herein. A summary of the terms and conditions of the Programme and the Bonds appears below. The applicable terms of any Bonds will be agreed between the Issuer and the relevant Dealer prior to the issue of the Bonds and will be set out in the Terms and Conditions of the Bonds endorsed on, attached to, or incorporated by reference into, the Bonds, as modified and supplemented by the applicable Final Terms attached to, or endorsed on, such Bonds, as more fully described in Chapter 8, “*Form of the Bonds*”.

This Prospectus and any supplement will only be valid for listing Bonds on the Official List during the period of 12 months from the date of this Prospectus in an aggregate nominal amount which, when added to the aggregate nominal amount then outstanding of all Bonds previously or simultaneously issued under the Programme, does not exceed €10,000,000,000 or its equivalent in other currencies. For the purpose of calculating the euro equivalent of the aggregate nominal amount of Bonds issued under the Programme from time to time:

- (i) the euro equivalent of Bonds denominated in another Specified Currency (as specified in the applicable Final Terms in relation to the Bonds, described in Chapter 8, “*Form of the Bonds*”) shall be determined, at the discretion of the Issuer, either as of the date on which agreement is reached for the issue of Bonds or on the preceding day on which commercial banks and foreign exchange markets are open for business in London, in each case on the basis of the spot rate for the sale of euro against the purchase of such Specified Currency in the London foreign exchange market quoted by any leading international bank selected by the Issuer on the relevant day of calculation;
- (ii) the euro equivalent of Dual Currency Bonds, Index Linked Bonds and Partly-Paid Bonds (each as specified in the applicable Final Terms in relation to the Bonds, described in Chapter 8, “*Form of the Bonds*”) shall be calculated in the manner specified above by reference to the original nominal amount on issue of such Bonds (in the case of Partly-Paid Bonds regardless of the subscription price paid); and
- (iii) the euro equivalent of Zero Coupon Bonds (as specified in the applicable Final Terms in relation to the Bonds, described in Chapter 8, “*Form of the Bonds*”) and other Bonds issued at a discount or a premium shall be calculated in the manner specified above by reference to the net proceeds received by the Issuer for the relevant issue.

## CHAPTER 1

### PARTIES

Account Bank:	Barclays Bank PLC, or any person for the time being acting as Account Bank pursuant to the Account Bank Agreement.
Arranger:	Barclays Bank PLC is the arranger of the Programme.
AWG:	AWG plc, a company incorporated under the laws of England and Wales which is admitted to the Official List of the United Kingdom Listing Authority and to trading on the London Stock Exchange, the ultimate holding company of the AWG Group.
AWG Group:	AWG and its subsidiaries (including Anglian Water).
AWG Group Ltd:	AWG Group Ltd (formerly Anglian Water Plc), a company incorporated under the laws of England and Wales and formerly listed on the London Stock Exchange and a wholly-owned subsidiary of AWG.
AW Group:	The group of companies of AWG Group Ltd and its subsidiaries prior to the introduction of AWG as parent company of AWG Group Ltd in 2000.
Anglian Water:	Anglian Water Services Limited, a water and sewerage undertaker under the Instrument of Appointment.
Anglian Water Services Financing Group:	Anglian Water Services Holdings Ltd, Anglian Water Services Overseas Holdings Ltd, Anglian Water and Anglian Water Services Financing Plc (the “ <b>Obligors</b> ”).
Anglian Water Services Holdings Ltd:	Anglian Water Services Holdings Limited, a company incorporated under the laws of England and Wales and a wholly-owned subsidiary of AWG Group Ltd.
Anglian Water Services Overseas Holdings Ltd:	Anglian Water Services Overseas Holdings Limited, a company incorporated in the Cayman Islands and a wholly-owned subsidiary of Anglian Water Services Holdings Ltd.
Authorised Credit Provider:	Barclays Bank PLC (the “ <b>Authorised Credit Facility Agent</b> ”) as agent in respect of the revolving working capital and capital expenditure credit facility (the “ <b>Authorised Loan Agreement</b> ”) provided to the Issuer by Barclays Bank PLC, syndicated to certain other banks or financial institutions (each an “ <b>Authorised Credit Provider</b> ”) which agreed to provide credit facilities to the Issuer and/or Anglian Water. See Chapter 7, “ <i>Financing Structure</i> ”. This Authorised Loan Agreement replaces the initial authorised loan agreement (the “ <b>Initial Authorised Loan Agreement</b> ”) provided to the Issuer by Barclays Bank PLC and syndicated to certain other banks (the “ <b>Initial Authorised Credit Providers</b> ”) on or about the Effective Date.
Bond Trustee:	Deutsche Trustee Company Limited for and on behalf of the holders of each Series of Bonds (each, a “ <b>Bondholder</b> ”).
Cash Manager:	Anglian Water (prior to a Standstill Period) and Barclays Bank PLC (during and following a Standstill Period) do and will, pursuant to the terms of the Common Terms Agreement, act as cash manager in respect of monies credited from time to time to the Accounts.
Common Depositary:	Deutsche Bank AG, London Branch acts as common depositary for Euroclear Bank S.A. / N.V. as operator of the Euroclear System and Clearstream Banking, société anonyme, in respect of the Programme.
Dealers:	Barclays Bank PLC, BNP Paribas, Citigroup Global Markets Limited, Deutsche Bank AG, London Branch, Dresdner Bank AG London Branch, HSBC Bank plc, Bayerische Hypo- und Vereinsbank AG, ING Bank N.V., J.P. Morgan

Securities Ltd. and The Royal Bank of Scotland plc will act as dealers (together with any other dealer appointed from time to time by the Issuer, (the “**Dealers**”)), in respect of the Programme.

Debt Service Reserve Liquidity Facility Providers:	Barclays Bank PLC, HSBC Bank plc and the Royal Bank of Scotland plc (the “ <b>Debt Service Reserve Liquidity Facility Provider</b> ”) agreed to provide a liquidity facility (the “ <b>Class A Debt Service Reserve Liquidity Facility</b> ”) for interest requirements on Class A Debt and (with the exception of HSBC Bank plc) a liquidity facility (the “ <b>Class B Debt Service Reserve Liquidity Facility</b> ”) for interest requirements on Class B Debt and (in certain circumstances) to fund shortfalls in the Class A Debt Service Reserve Account (each a “ <b>Debt Service Reserve Liquidity Facility</b> ”).
Finance Lessors:	Each of Mercantile Leasing Company (No. 132) Limited, D-LAF Limited or Moon Leasing Limited (in its capacity as General Partner of Brahms Leasing Limited Partnership), Deutsche Bank AG, London Branch, CSC Computer Sciences Limited and Barclays Technology Finance Limited (together the “ <b>Existing Finance Lessors</b> ”), which lease plant, machinery and equipment to Anglian Water, under the terms of various finance leases (the “ <b>Existing Finance Leases</b> ”) (and, together with Barclays Technology Finance Limited and any future finance leases, the “ <b>Finance Leases</b> ”).
Financial Guarantors:	MBIA Assurance S.A. (“ <b>MBIA</b> ”) as initial financial guarantor (in such capacity, the “ <b>Initial Financial Guarantor</b> ”) has issued in respect of Class A Wrapped Bonds on the Effective Date and may, under the terms of financial guarantee insurance policies (and subject to the satisfaction of certain conditions), agree to issue in favour of the Bond Trustee in respect of such further Class A Wrapped Bonds and/or Class B Wrapped Bonds, financial guarantee insurance policies (together with any other financial guarantee insurance policies issued by other Financial Guarantors, the “ <b>Bond Policies</b> ”). The Bond Policies do, in respect of Class A Wrapped Bonds in issue and will, in respect of further Class A Wrapped Bonds and/or Class B Wrapped Bonds, unconditionally and irrevocably guarantee the scheduled payment of interest and principal (as adjusted for indexation but excluding certain amounts including additional amounts relating to prepayment or any accelerated amounts or amounts by which the interest coupons on such Bonds exceeds the initial coupon on such Bonds as at the date on which such Bonds were issued (together, the “ <b>FG Excepted Amounts</b> ”)) in respect of such Class A Wrapped Bonds and/or Class B Wrapped Bonds. As the existing MBIA commitment has been fully utilised, no information is included in this Prospectus in relation to MBIA. Subject to the approval of the Dealers and confirmation of no downgrade of the Wrapped Bonds in issue from at least two of the Rating Agencies, the Issuer may arrange for any financial institution to issue Bond Policies in respect of further Series of Class A Wrapped Bonds and/or Class B Wrapped Bonds (or further Class A Wrapped Debt and/or Class B Wrapped Debt, as the case may be) (each such financial institution, a “ <b>Financial Guarantor</b> ”). For the avoidance of doubt, the Issuer may not as of the date of this Prospectus issue Wrapped Bonds pursuant to this Prospectus. If in the future any Financial Guarantor (as defined below) shall have a commitment in relation to the Programme which is available and to be utilised then this Prospectus shall be updated to include information on such Financial Guarantor.
Hedge Counterparties:	Barclays Bank PLC of 5 The North Colonnade, Canary Wharf, London E14 4BB, Citibank, N.A., London Branch of 33 Canada Square, Canary Wharf, London E14 5LB, Deutsche Bank AG, London Branch of Head Office, Taunusanlage 12, 60262 Frankfurt, Germany, Dresdner Bank AG of Jürgen-Ponto Platz 1, D60301 Frankfurt/Main, Germany, HSBC Bank plc of Thames Exchange, 10 Queen Street Place, London EC4R 1BQ and The Royal Bank of Scotland plc of RBS Financial Markets, Level 4, 135 Bishopsgate, London

EC2M 3UR (together the “**Existing Hedge Counterparties**” and, together with BNP Paribas, 75450 Paris Cedex 09, France, Morgan Stanley & Co. International Limited, 25 Cabot Square, London E14 4QA, SMBC Capital Markets, Inc., 277 Park Avenue, Fifth Floor, New York, New York 10172, USA and any future counterparties to Hedging Agreements, the “**Hedge Counterparties**”).

Issuer:	Anglian Water Services Financing Plc, formed in order to provide debt financing to Anglian Water in relation to its water and sewerage undertakings.
O&M Reserve Facility Provider:	Barclays Bank PLC, The Royal Bank of Scotland plc and BNP Paribas (together, the “ <b>O&amp;M Reserve Facility Provider</b> ”) agreed to provide a liquidity facility in respect of operating and maintenance expenditure (the “ <b>O&amp;M Reserve Facility</b> ”).
Obligors:	The following parties have guaranteed and will guarantee certain obligations of each other Obligor in favour of the Security Trustee (for itself and on behalf of the Secured Creditors): (i) Anglian Water Services Holdings Ltd, (ii) Anglian Water Services Overseas Holdings Ltd, (iii) Anglian Water and (iv) the Issuer (each, an “ <b>Obligor</b> ”).
Principal Paying Agent:	Deutsche Bank AG, London Branch acts as issuing and principal paying agent and provides certain paying agency services to the Issuer in respect of Bearer Bonds.
Registrar and Exchange Agent:	Deutsche Bank Trust Company Americas acts as registrar and exchange agent and provides certain registrar and exchange agent services to the Issuer in respect of Registered Bonds.
Secured Creditors:	means any person who is a party to, or who has acceded to, the STID (as defined in Chapter 18, “ <i>Index of Defined Terms</i> ”) as a Secured Creditor.
Security Trustee:	Deutsche Trustee Company Limited acts as security trustee and holds, and is entitled to enforce (for itself and on behalf of the Secured Creditors), the Security.
Transfer Agent:	Deutsche Bank AG, London Branch acts as transfer agent and provides certain transfer agency services to the Issuer in respect of the Registered Bonds.

## CHAPTER 2

### OVERVIEW OF THE PROGRAMME

*The following summary does not purport to be complete and is taken from, and is qualified in its entirety by, the remainder of this Prospectus and, in relation to the terms and conditions of any particular Tranche of Bonds, the applicable Final Terms. Words and expressions not defined in this summary shall have the same meanings as defined in Chapter 8, “**Form of the Bonds**” and in Chapter 9, “**Terms and Conditions of the Bonds**”.*

Description:	Global Secured Medium Term Note Programme
Programme Size:	Up to €10,000,000,000 (or its equivalent in other currencies calculated as described under “ <i>General Description of the Programme</i> ” below) aggregate nominal amount of Bonds outstanding at any time.
Issuance in Classes:	<p>Bonds issued under the Programme have and will be issued in series (each a “<b>Series</b>”), with each Series belonging to one of 4 classes (each a “<b>Class</b>”). The Wrapped Bonds are and will be designated as either “<b>Class A Wrapped Bonds</b>” or “<b>Class B Wrapped Bonds</b>”. The Unwrapped Bonds are and will be designated as one of “<b>Class A Unwrapped Bonds</b>” or “<b>Class B Unwrapped Bonds</b>”. Each Series comprises or will comprise one or more Tranches (each a “<b>Tranche</b>”) of Bonds, the specific terms of each Tranche being identical in all respects save for the issue dates, interest commencement dates and/or issue prices, to the terms of other Tranches of the same Series.</p> <p>The specific terms of each Tranche of Bonds are and will be set out in the applicable Final Terms.</p>
Issue Dates:	23 July 2002 (the “ <b>Initial Issue Date</b> ”) and thereafter on such dates (each an “ <b>Issue Date</b> ”) as agreed between the Issuer and the Dealers.
Certain Restrictions:	<p>Each issue of Bonds denominated in a currency in respect of which particular laws, guidelines, regulations, restrictions or reporting requirements apply will only be issued in circumstances which comply with such laws, guidelines, regulations, restrictions or reporting requirements from time to time including the following restrictions applicable at the date of this Prospectus. See Chapter 15, “<i>Subscription and Sale and Transfer and Selling Restrictions</i>”.</p> <p><b>Bonds with a maturity of less than one year</b></p> <p>Bonds issued on terms that they must be redeemed before their first anniversary will constitute deposits for the purposes of the prohibition on accepting deposits contained in Section 19 of the Financial Services and Markets Act 2000 unless they are issued to a limited class of professional investors and have a denomination of at least £100,000 or its equivalent. See Chapter 15, “<i>Subscription and Sale and Transfer and Selling Restrictions</i>”.</p>
Distribution:	Bonds have and may be distributed by way of private or public placement and in each case on a syndicated or non-syndicated basis.
Currencies:	Bonds in issue are, and any further Bonds issued under the Programme will be denominated in euro, Sterling, U.S. dollars, yen and, subject to any applicable legal or regulatory restrictions, any other currency agreed between the Issuer and the relevant Dealer.
Redenomination:	The applicable Final Terms may provide that certain Bonds may be redenominated in euro. The relevant provisions applicable to any such redenomination will be contained in Condition 6, as amended by the applicable Final Terms.

Maturities:	Such maturities as may be agreed between the Issuer and the relevant Dealer, subject to such minimum or maximum maturities as may be allowed or required from time to time by the relevant central bank (or equivalent body) or any laws or regulations applicable to the Issuer or the relevant Specified Currency.
Issue Price:	Bonds have and may be issued on a fully-paid or a partly-paid basis and at an issue price which is at par or at a discount to, or premium over, par, as specified in the relevant Final Terms.
Form of Bonds:	The Bonds in issue have been issued under the Programme in bearer form. Further Bonds issued under the Programme will be issued in bearer or registered form as described in Chapter 8, “ <i>Form of the Bonds</i> ”. Registered Bonds will not be exchangeable for Bearer Bonds and vice versa.
Fixed Rate Bonds:	Fixed interest is and will be payable on such date or dates as may be agreed between the Issuer and the relevant Dealer and on redemption and will be calculated on the basis of such Day Count Fraction as may be agreed between the Issuer and the relevant Dealer (as specified in the relevant Final Terms).
Floating Rate Bonds:	<p>Floating Rate Bonds do and will bear interest at a rate determined:</p> <ul style="list-style-type: none"> <li>(i) on the same basis as the floating rate under a notional interest rate swap transaction in the relevant Specified Currency governed by an agreement incorporating the 2000 ISDA Definitions (as published by the International Swaps and Derivatives Association, Inc., and as amended and updated as at the Issue Date of the first Tranche of the Bonds of the relevant Series); or</li> <li>(ii) on the basis of a reference rate appearing on the agreed screen page of a commercial quotation service; or</li> <li>(iii) on such other basis as may be agreed between the Issuer and the relevant Dealer.</li> </ul> <p>The margin (if any) relating to such floating rate will be agreed between the Issuer and the relevant Dealer for each Series of Floating Rate Bonds (as specified in the relevant Final Terms).</p>
Index Linked Bonds:	<p>Payments of principal in respect of Index Linked Redemption Bonds or of interest in respect of Index Linked Interest Bonds is and will be calculated by reference to such index and/or formula or to changes in the prices of securities or commodities or to such other factors as the Issuer and the relevant Dealer have agreed and may agree.</p> <p>Index Linked Bonds which are issued as an appel public à l’épargne in France must be issued in compliance with the Principes Généraux from time to time set by the Commission des Opérations de Bourse and the Conseil des Bourses de Valeurs or any successor body thereto.</p>
Other provisions in relation to Floating Rate Bonds and Index Linked Interest Bonds:	<p>Floating Rate Bonds and Index Linked Interest Bonds may also have a maximum interest rate, a minimum interest rate or both.</p> <p>Interest on Floating Rate Bonds and Index Linked Interest Bonds in respect of each Interest Period, as agreed prior to issue by the Issuer and the relevant Dealer, is and will be payable on such Interest Payment Dates, and will be calculated on the basis of such Day Count Fraction, as has been and may be agreed between the Issuer and the relevant Dealer.</p>
Indexation Bonds:	Payments of interest and principal in respect of Indexation Bonds are and will be adjusted for indexation by reference to the relevant Index Ratio.



Dual Currency Bonds:	Payments (whether in respect of principal or interest and whether at maturity or otherwise) in respect of Dual Currency Bonds will be made in such currencies, and based on such rates of exchange, as the Issuer and the relevant Dealer may agree.
Zero Coupon Bonds:	Zero Coupon Bonds will be offered and sold at a discount to their nominal amount and will not bear interest.
Redemption:	<p>The applicable Final Terms indicate and will indicate either that the relevant Bonds cannot be redeemed prior to their stated maturity (other than in specified instalments, or for taxation reasons if applicable, or following an Event of Default) or that such Bonds are or will be redeemable at the option of the Issuer and/or the Bondholders upon giving notice to the Bondholders or the Issuer, as the case may be, on a date or dates specified prior to such stated maturity and at a price or prices and on such other terms as may be agreed between the Issuer and the relevant Dealer, in each case as set out in the applicable Final Terms.</p> <p>The applicable Final Terms may provide that Bonds may be redeemable in two or more instalments of such amounts and on such dates as are indicated in the applicable Final Terms.</p> <p>Bonds issued on terms that they must be redeemed before their first anniversary are subject to restrictions on their denomination and distribution, see “<i>Certain Restrictions – Bonds with a maturity of less than one year</i>” above.</p> <p>The Financial Guarantors do not and will not guarantee any of the amounts payable by the Issuer upon an early redemption, and their obligation is and will be to continue to make payments in respect of the Bonds pursuant to the relevant Bond Policy on the dates on which such payments would have been required to be made had such early redemption not occurred.</p> <p>The Issuer is only permitted to pay Early Redemption Amounts to the extent that in so doing it will not cause an Event of Default to occur or subsist.</p>
Denomination of Bonds:	<p>Bonds have and will be issued in such denominations as have been and may be agreed between the Issuer and the relevant Dealer save that (i) in the case of any Bonds which are to be admitted to trading on a regulated market within the European Economic Area or offered to the public in a Member State of the European Economic Area in circumstances which require the publication of a prospectus under the Prospectus Directive, the minimum denomination shall be €50,000 (or its equivalent in any other currency as at the date of issue of the Bonds); and (ii) the minimum denomination of each Bond is and will be such as may be allowed or required from time to time by the relevant central bank (or equivalent body) or any laws or regulations applicable to the relevant Specified Currency, see “<i>Certain Restrictions – Bonds with a maturity of less than one year</i>” above.</p> <p>Unless otherwise stated in the applicable Final Terms, the minimum denomination of each Definitive IAI Registered Bond will be U.S.\$500,000 or its approximate equivalent in other Specified Currencies.</p>
Taxation:	Payments in respect of Bonds or under the relevant Bond Policy are and will be made without withholding or deduction for, or on account of, any present or future taxes, duties, assessments or governmental charges of whatever nature imposed or levied by or on behalf of any jurisdiction, unless and save to the extent that the withholding or deduction of such taxes, duties, assessments or governmental charges is required by law. In that event and to that extent, the Issuer and, to the extent there is a claim under the relevant Bond Policy, the relevant Financial Guarantor will make payments subject to the appropriate withholding or deduction. No additional amounts are or will be paid by the Issuer or, to the extent there is a claim under the relevant Bond Policy, by the

relevant Financial Guarantor in respect of any withholdings or deductions, unless otherwise specified in the applicable Final Terms.

- Status of the Bonds: The Bonds in issue constitute and any further Bonds issued under the Programme will constitute, secured obligations of the Issuer. Each Class of Bonds in issue ranks, and any further Class of Bonds issued under the Programme will rank, *pari passu* without preference or priority in point of security amongst themselves.
- The Bonds represent the right of the holders of such Bonds to receive interest and principal payments from (a) the Issuer in accordance with the Terms and Conditions of the Bonds (the “**Conditions**”) and the trust deed (the “**Bond Trust Deed**”) entered into by the Obligors, MBIA and the Bond Trustee in connection with the Programme and (b) in the case of the Wrapped Bonds only, the relevant Financial Guarantor in certain circumstances in accordance with the relevant Bond Policy.
- The Class A Wrapped Bonds and the Class A Unwrapped Bonds in issue rank, and any further Class A Wrapped Bonds and Class A Unwrapped Bonds issued under the Programme will rank, *pari passu* with respect to payments of interest and principal. However, only the Class A Wrapped Bonds have the benefit of the relevant Bond Policy. All claims in respect of the Class A Wrapped Bonds and the Class A Unwrapped Bonds in issue rank, and any further Class A Wrapped Bonds and Class A Unwrapped Bonds issued under the Programme will rank, in priority to payments of interest and principal due on all Class B Wrapped Bonds and Class B Unwrapped Bonds.
- The Class B Wrapped Bonds and the Class B Unwrapped Bonds in issue rank, and any further Class B Wrapped Bonds and Class B Unwrapped Bonds issued under the Programme will rank, *pari passu* with respect to payments of interest and principal. However, only the Class B Wrapped Bonds will have the benefit of the relevant Bond Policy.
- Covenants: The representations, warranties, covenants (positive, negative and financial) and events of default which will apply to, *inter alia*, the Bonds are set out in a Common Terms Agreement dated 30 July 2002 (the “**Common Terms Agreement**”).
- Guarantee and Security: The Bonds in issue are and further Bonds issued under the Programme will be, unconditionally and irrevocably guaranteed and secured by each Obligor pursuant to a guarantee and security agreement (the “**Security Agreement**”) entered into by each Obligor in favour of the Security Trustee over the entire property, assets, right and undertaking of each Obligor (the “**Security**”), in the case of Anglian Water to the extent permitted by the WIA and Licence. Each such guarantee constitutes a direct, unconditional and secured obligation of each Obligor. The Security is held by the Security Trustee on trust for the Secured Creditors (as defined below) under the terms of the Security Agreement, subject to the terms of the STID (as defined below).
- Intercreditor Arrangements: The Secured Creditors are each party to a security trust and intercreditor deed (the “**STID**”), which regulates, *inter alia*, (i) the claims of the Secured Creditors; (ii) the exercise and enforcement of rights by the Secured Creditors; (iii) the rights of the Secured Creditors to instruct the Security Trustee; (iv) the rights of the Secured Creditors during the occurrence of an Event of Default; (v) the Entrenched Rights and Reserved Matters of each Secured Creditor; and (vi) the giving of consents and waivers and the making of amendments by the Secured Creditors. See Section 7.3, “*Financing Structure – Security Trust and Intercreditor Deed*”.
- Status of Bond Policies: Each financial guarantee insurance policy (each a “**Bond Policy**”) issued in favour of the Bond Trustee in relation to each Tranche of Wrapped Bonds in

issue and any further Tranche of Wrapped Bonds, constitutes and will constitute, an unsubordinated and unsecured obligation of the relevant Financial Guarantor, save for certain mandatory exceptions provided by law, pursuant to which the relevant Financial Guarantor does and will guarantee the timely payment of interest and principal (other than the FG Excepted Amounts) on the relevant Tranche of Wrapped Bonds.

- Counter Indemnity: The Issuer is obliged, pursuant to the terms of an insurance and indemnity agreement with the relevant Financial Guarantor, *inter alia*, to reimburse such Financial Guarantor in respect of payments made by it under the relevant Bond Policy or Bond Policies. Each such Financial Guarantor is and will be subrogated to the rights of the relevant Class A Wrapped Bondholders or Class B Wrapped Bondholders, as the case may be, against the Issuer in respect of any payments made under such Bond Policies. See Section 7.8, “*Financing Structure – Financial Guarantor Documents*”.
- Authorised Credit Facilities: Subject to certain conditions being met, the Issuer is permitted to incur indebtedness, including lease finance, under authorised credit facilities (each an “**Authorised Credit Facility**”) with an Authorised Credit Provider, providing loan, hedging and other facilities. Each Authorised Credit Provider will be party to the CTA and the STID and may have voting rights thereunder. See Chapter 7, “*Financing Structure*”.
- Debt Service Reserve Liquidity Facilities: The Debt Service Reserve Liquidity Facility Providers make available to the Issuer two 364-day credit facilities for the purpose of meeting certain shortfalls in revenues: (i) for the Issuer to meet (*inter alia*) its obligations to pay interest on the Bonds or (ii) to make payments under any Authorised Credit Facilities entered. The Issuer is obliged, pursuant to the CTA, to enter into new, or increase its existing liquidity facilities each time it issues further Class A Debt or Class B Debt.
- O&M Reserve Facilities: The O&M Reserve Facility Provider has made available to the Issuer a liquidity facility for the purpose of meeting operating and maintenance expenses.
- Listing: The Bonds issued on the Initial Issue Date and all subsequent issues under the Programme have been admitted to the Official List and admitted to trading on the Market and an application will be made to admit any additional Bonds issued under the Programme to the Official List and to admit them to trading on the Market. Any additional Bonds may also be listed on such other or further stock exchange(s) as may be agreed between the Issuer and the relevant Dealer in relation to each Series.
- Unlisted Bonds may also be issued. The applicable Final Terms will state whether or not the relevant Bonds are to be listed and, if so, on which stock exchange(s).
- Ratings: The ratings assigned to Class A Wrapped Bonds in issue are, and in respect of any further Class A Wrapped Bonds and Class B Wrapped Bonds will be, based solely on the debt rating of a Financial Guarantor appointed and reflect only the views of the Rating Agencies. The ratings assigned to the Class A Unwrapped Bonds and the Class B Unwrapped Bonds by the Rating Agencies reflect only the views of the Rating Agencies. The ratings will be specified in the relevant Final Terms.
- A rating is not a recommendation to buy, sell or hold securities and will depend, amongst other things, on certain underlying characteristics of the business and financial condition of Anglian Water or, in the case of the Class A Wrapped Bonds and/or Class B Wrapped Bonds, of a Financial Guarantor from time to time. A rating may be subject to suspension, change or withdrawal at any time by the assigning Rating Agency.**

Governing Law:	The Bonds in issue and any further Bonds issued under the Programme will be governed by, and construed in accordance with, English law.
Selling Restrictions:	There are restrictions on the offer, sale and transfer of the Bonds in the United States, the United Kingdom, the Cayman Islands, Japan, The Netherlands and Germany and such other restrictions as may be required in connection with the offering and sale of a particular Tranche of Bonds. See Chapter 15, “ <i>Subscription and Sale and Transfer and Selling Restrictions</i> ”.
United States Selling Restrictions:	Regulation S (Category 2), Rule 144A or Section 4(2), TEFRA C or TEFRA D as specified in the applicable Final Terms. See Chapter 15, “ <i>Subscription and Sale and Transfer and Selling Restrictions</i> ”.

## CHAPTER 3

### MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

In the management's discussion and analysis and related financial information set forth below, references to Anglian Water in respect of each of the years ended 31 March 2005, 2004 and 2003 are to Anglian Water and its subsidiary undertakings.

The financial information set forth below has been extracted without material adjustment from, and together with management's discussion and analysis set forth below should be read in conjunction with, the audited consolidated financial statements of Anglian Water for the years ended 31 March 2005, 2004 and 2003.

The consolidated financial statements of Anglian Water have been prepared in accordance with U.K. GAAP. Certain significant differences exist between U.K. GAAP and U.S. GAAP which might be material to the financial information herein. Anglian Water has made no attempt to identify or quantify the impact of those differences. Potential investors should consult their own professional advisers for an understanding of the differences between U.K. GAAP and U.S. GAAP, and how those differences might affect the financial information herein. See Chapter 17, "*Summary of Certain Significant Differences Between U.K. GAAP and U.S. GAAP*". In making an investment decision, investors must rely upon their own examination of Anglian Water, the terms of the offering and the financial information.

## Profit and Loss Data

	<i>For the year ended 31 March</i>		
	2005	2004	2003
	£m	£m	£m
<b>Turnover – continuing operations</b> .....	796.8	766.6	726.8
Operating costs:			
Operating costs before depreciation.....	(291.1) <sup>(1)</sup>	(291.7) <sup>(2)</sup>	(301.1) <sup>(3)</sup>
Depreciation net of amortisation of grants and contributions .	(166.4)	(156.0)	(156.9)
<b>Total operating costs</b> .....	(457.5)	(447.7)	(458.0)
<b>Operating profit – continuing operations</b> .....	339.3	318.9	268.8
Profit on disposal of business.....	—	—	3.3 <sup>(4)</sup>
Profit on sale of fixed assets .....	—	—	0.6 <sup>(5)</sup>
<b>Profit on ordinary activities before interest</b> .....	339.3	318.9	272.7
Interest payable (net) .....	(61.4)	(49.7)	(105.8) <sup>(6)</sup>
<b>Profit on ordinary activities before taxation</b> .....	277.9	269.2	166.9
Tax on profit on ordinary activities .....	(12.4)	33.5 <sup>(7)</sup>	(57.7) <sup>(8)</sup>
<b>Profit on ordinary activities after taxation for the financial year</b> .....	265.5	302.7	109.2
Dividends paid/payable .....	(253.1)	(250.6)	(510.6)
<b>Profit for the financial year</b> .....	12.4	52.1	619.8

### Notes:

- (1) Includes £11.4 million of restructuring costs.
- (2) Includes £4.7 million of restructuring costs.
- (3) Includes £18.6 million of costs treated as exceptional operating costs, comprising £15.7 million of refinancing project costs and £2.9 million of restructuring costs.
- (4) Profit resulting from the sale of certain non-trading companies to AWG Group Ltd.
- (5) Profit resulting from the sale of surplus land and assets.
- (6) Includes an exceptional interest charge of £49.6 million relating to a provision of £32.0 million for coupon enhancement costs on debt transferred to Anglian Water and £17.6 million of other one-time costs relating to early termination of existing debt and bankers' fees arising from the refinancing and financial restructuring project of Anglian Water completed on 30 July 2002.
- (7) Includes a £22.2 million credit in respect of previous periods' corporation tax and an £11.3 million credit for deferred tax.
- (8) Includes a £37.8 million corporation tax charge and a £19.9 million charge relating to deferred tax.

**Balance Sheet Data***At 31 March*

	2005 £m	2004 £m	2003 £m
<b>Fixed assets</b>			
Tangible assets.....	3,911.4	3,801.5	3,696.7
Investments .....	1,609.2	1,609.3	1,609.3
	<u>5,520.6</u>	<u>5,410.8</u>	<u>5,306.0</u>
<b>Current assets</b>			
Stocks .....	6.9	6.6	4.6
Debtors .....	260.4	253.0	264.2
Investment-money market deposits.....	95.8	—	—
Cash at bank and in hand.....	744.0	471.7	176.9
	<u>1,107.1</u>	<u>731.3</u>	<u>445.7</u>
<b>Creditors: amounts falling due within one year</b>			
Short-term borrowings.....	(88.1)	(22.0)	(27.4)
Other creditors .....	(382.4)	(344.1)	(449.7)
	<u>(470.5)</u>	<u>(366.1)</u>	<u>(477.1)</u>
Net current assets/(liabilities).....	636.6	365.2	(31.4)
Total assets less current liabilities .....	<u>6,157.2</u>	<u>5,776.0</u>	<u>5,274.6</u>
<b>Creditors: amounts falling due after more than one year</b>			
Loans and other borrowings.....	(4,251.1)	(3,900.6)	(3,438.9)
Other creditors .....	(98.4)	(90.0)	(87.4)
	<u>(4,349.5)</u>	<u>(3,990.6)</u>	<u>(3,526.3)</u>
<b>Provisions for liabilities and charges .....</b>	<u>(158.9)</u>	<u>(149.0)</u>	<u>(164.0)</u>
	<u>1,648.8</u>	<u>1,636.4</u>	<u>1,584.3</u>
<b>Capital and reserves</b>			
Called up share capital .....	860.0	860.0	860.0
Profit and loss account .....	788.8	776.4	724.3
<b>Total shareholder's funds (all equity).....</b>	<u>1,648.8</u>	<u>1,636.4</u>	<u>1,584.3</u>

## Cash Flow Data

At 31 March

	2005	2004	2003
	£m	£m	£m
<b>Net cash inflow from operating activities</b> .....	512.9	484.0	415.9
<b>Returns on investments and servicing of finance</b>			
Interest received.....	214.4	206.5	95.5
Interest paid .....	(231.4)	(211.7)	(126.6)
Cash flows treated as finance costs under FRS 4 .....	(0.3)	(1.3)	(23.8)
Interest element of finance lease rental payments .....	(8.0)	(9.1)	(9.7)
Net cash outflow for returns on investments and servicing of finance .....	(25.3)	(15.6)	(64.6)
<b>Taxation</b>			
Corporation Tax (paid)/received .....	(0.8)	0.3	0.5
<b>Capital expenditure and financial investment</b>			
Purchase of tangible fixed assets .....	(290.9)	(276.6)	(261.7)
Grants and contributions received.....	26.9	18.6	17.0
Decrease in short-term loan to group company, AWG Group Ltd .....	—	—	309.5
Loan to group company, Anglian Water Services Holdings Ltd .....	—	—	(1,609.1)
Disposal of tangible fixed assets.....	1.1	1.1	1.3
Net cash outflow for capital expenditure and financial investment .....	(262.9)	(256.9)	(1,543.0)
<b>Acquisitions and disposals</b>			
Receipt from sale of fixed asset investment.....	0.1	—	—
Acquisition of trade and certain assets of a group company, Geodesys Limited (net of cash acquired).....	—	—	1.7
Net cash inflow for acquisitions and disposals .....	0.1	—	1.7
<b>Equity dividends paid</b> .....	(233.6)	(345.1)	(136.0)
<b>Net cash outflow before management of liquid resources and financing</b> .....	(9.6)	(133.3)	(1,325.5)
<b>Management of liquid resources</b>			
Increase in short-term deposits and investments.....	(503.4)	(180.8)	(88.2)
<b>Financing</b>			
Increase in loans .....	398.3	453.2	1,947.3
Repayments of amounts borrowed.....	(3.3)	(0.7)	(255.1)
Capital element of finance lease rental payments.....	(17.3)	(24.4)	(21.7)
<b>Net cash inflow from financing</b> .....	377.7	428.1	1,670.5
<b>(Decrease)/increase in cash</b> .....	(135.3)	114.0	256.8



## Management's Discussion and Analysis of Financial Condition and Results of Operations

### Overview

Anglian Water conducts the UK regulated water and sewerage activities of the AWG Group. Anglian Water's principal activities in the water business include the abstraction, storage, treatment and distribution of water to residential, commercial and industrial customers. Anglian Water's principal activities in the sewerage business involve the collection, treatment and disposal of domestic sewage, trade effluent and water through its network of sewers and treatment plants. As at the date of this Prospectus, Anglian Water served the largest geographic area of the regional water and sewerage companies in England and Wales, providing water services to approximately 4.2 million people in an area covering approximately 22,000 square kilometres and sewerage services to approximately 5.9 million people in an area covering approximately 27,500 square kilometres.

### Factors Affecting Financial Condition and Results of Operations

#### Regulation

Anglian Water operates within a highly regulated industry in England and Wales. Anglian Water's turnover, operating costs and investment decisions are heavily influenced by the regulated tariff rates which Anglian Water may charge its customers as established by its economic regulator, the Director General of Water Services ("DGWS") (who is assisted in his duties by Ofwat), as well as environmental regulation and the terms of its Licence. Every five years, the DGWS sets a price limit intended to enable water and sewerage companies in England and Wales to finance operations and earn a reasonable return on capital. The pricing regime administered by the DGWS provides for interim reviews in specified, limited circumstances. Recent legislation provides that the DGWS and Ofwat are to be replaced by a new body, the Water Services Regulation Authority (the "WSRA"). From the moment it is established, which is expected to occur in 2006, the WSRA will have the DGWS's power to set price limits.

On 25 November 1999, Ofwat published its final determination of tariff rates chargeable by Anglian Water in respect of the five-year period between 2000 and 2005. Under the agreed price determination, DGWS permitted Anglian Water to increase its annual average price before adjustment for inflation by 2.5 per cent. in both 2003 to 2004 and 2004 to 2005. On 2 December 2004, Ofwat published its final determination of the new tariff rates chargeable by Anglian Water over the five-year period between 2005 and 2010. The revised price limits, which came into effect on 1 April 2005, resulted in an initial increase of 3.8 per cent. in the weighted average value (before adjustment for inflation) of Anglian Water's customer bills for 2005 to 2006. For additional information on the price limit mechanism, including provisions for adjustments, and on regulation of the water and sewerage industry generally, see Chapter 4, "*Anglian Water Business Description*" and Chapter 11, "*Regulation of the Water and Sewerage Industry in England and Wales*".

#### Metering

Another trend which has influenced and is likely to continue to significantly influence Anglian Water's turnover and operating costs is the growth in the number of residential customers in Anglian Water's water supply and sewerage licence areas who pay for water supply and sewerage services on the basis of actual usage as measured by installed water meters. Historically, water supply and sewerage services in England and Wales were charged on the basis of fixed tariffs based on property values. However, the water regulators in England and Wales perceived metering as a beneficial development for consumers, as it promotes greater transparency between price and usage. Operating costs associated with metered customers, such as the cost of reading meters, billing metered customers and responding to customer queries, are significantly higher than for unmetered customers. According to data published by Ofwat, over the seven-year period between 1998 and 2005, the number of metered households in England and Wales rose from 2.3 million in 1998 (or approximately 11.0 per cent. of households) to 5.6 million in 2005 (or approximately 26.0 per cent. of households). In Anglian Water's water supply and sewerage licence areas, the number of metered households rose from 0.5 million in 1998 (or 31.0 per cent. of households) to 1.0 million in 2005 (or 54.0 per cent. of households).

Typically, the transition by customers towards metered water results in lower aggregate volumes of reported water used and consequently lower gross revenues in periods immediately following the transition, because customers' bills are directly linked to usage. However, reductions in usage are factored into the regulatory pricing model, based on projections of numbers of customers and their characteristics as agreed with the DGWS. See Chapter 11, "*Regulation of the Water and Sewerage Industry in England and Wales*". The principal risk to a regulated water and sewerage company's revenues is that actual numbers of customers switching to meters or other reductions in consumption patterns are greater than anticipated in the price model. Anglian Water has had a longer track record with a relatively higher proportion of metered customers than other

water companies and the Directors believe this experience has helped reduce its risks of inaccurately forecasting the growth in metered customers and their consumption patterns. See Chapter 4, “*Anglian Water Business Description*” and Chapter 6, “*Risk Factors*” and in particular, Section 6.1.2, “*Risk Factors – Water Act and Competition in the Water Industry*” and Section 6.2, “*Risk Factors – Anglian Water Revenue Considerations*”.

### ***Competition***

Anglian Water currently has a virtual monopoly over water supply and sewerage services within its licence areas. In recent years, the UK Government and Ofwat have pursued a number of initiatives to increase competition in the water and sewerage industry including: facilitating so-called “inset” appointments, which allow a company to provide water or sewerage services within another company’s water supply or sewerage licence areas; securing competition in the provision of water mains and service pipes; facilitating common carriage, for example, by developing access codes to set out fair terms for common carriage using others’ networks; and using the competition law powers under the Competition Act 1998 to prevent abuses of a dominant position and anti-competitive behaviour. The Water Act contains provisions which aim to increase the opportunities for competition in the supply of water services to eligible non-residential users of large amounts of water (at least 50 megalitres of water a year). In addition, the Water Act has introduced licences for new entrants, which puts common carriage on a statutory basis, including a “retail only” licence whereby the new entrant will purchase water on a wholesale basis from the existing water undertaker and then make a retail supply to the customer. Increased competition could affect Anglian Water’s virtual monopoly within its region, but it will continue to be able to compete for customers outside its licensed water supply and sewerage areas by applying for an inset. Moreover, the Directors believe that the Water Act’s competition-related provisions will have a limited impact on Anglian Water’s competitive position as the bulk of Anglian Water’s turnover derives from residential customers and not non-residential, high usage customers. See Section 6.1.2, “*Risk Factors – Water Act and Competition in the Water Industry*” and Chapter 11, “*Regulation of the Water and Sewerage Industry in England and Wales*” and in particular Sections 11.10.1 and 11.10.2, “*Regulation of the Water and Sewerage Industry in England and Wales – Competition in the Water Industry – General*” and “*– The Water Act*”.

### ***Economic and Demographic Trends***

The population of Anglian Water’s water supply and sewerage licence areas was comparatively stable over the last regulatory price review period (with an average growth rate of approximately 0.5 per cent. per year between 1996 and 2005). Moreover, steady growth in the population and new housing construction (which requires connection to the water and sewerage networks) have been factored into Anglian Water’s turnover forecasts. However, significant changes in macro-economic indicators, such as inflation and employment, could affect levels of new housing construction, reduce the population of the region as well as individual consumption and materially adversely affect Anglian Water’s business.

### **Turnover and Expenses**

The principal sources of Anglian Water’s turnover and expenses are as follows:

#### ***Turnover***

Anglian Water earns revenue for delivering treated water supplies to residential, commercial and large industrial customers and removing and treating sewage and other effluvia through its sewage network. Turnover is accounted for using standard accounting practices under U.K. GAAP. Turnover generally represents the income receivable (excluding value added tax (“VAT”)) in the ordinary course of business for services provided. Income receivable is based on the actual billing for the financial year to the end of the accounting period with an accrual or adjustment at the end of that period. For example, in the case of income from metered users, there is an accrual for income due but not billed based on average customer consumption data. This accrual is subsequently reconciled to actual billing, which takes place over the subsequent six months. See Anglian Water’s 2004 Annual Report and 2005 Annual Report. In the case of unmetered income which is billed in advance (principally at the start of the financial year) an adjustment is made at the end of each accounting period to take account of the income billed in advance for the subsequent accounting period. Other income (such as charges for connecting customers to Anglian Water’s water network) follow these general principles.

#### ***Operating Costs***

Historically, the principal component of Anglian Water’s operating costs is staff costs, which consist of wages and salaries, social security expenses and pension costs. The other major components of Anglian Water’s operating costs are raw materials and consumables, which consist of the various inputs required to deliver Anglian Water’s water and sewerage services (such as power, cement and chemicals).

### ***Depreciation***

For purposes of its statutory accounts (which Anglian Water is required to prepare in compliance with U.K. GAAP (the “**Statutory Accounts**”)), Anglian Water depreciates its assets in a manner that the Directors believe is consistent with that of other regulated water supply and sewerage companies in England and Wales. Depreciable assets are classified as either infrastructure assets (mains, sewers, reservoirs, dams, sludge pipelines and sea outfalls) and other assets (land and non-operational buildings, operational assets and vehicles, and plant and equipment). In accordance with accepted practice in the water industry in England and Wales, grants and capital contributions received in respect of infrastructure assets are deducted from the cost of these assets. The depreciation charge for infrastructure assets is the estimated level of annual expenditure required to maintain the operating capability of the network which is based on Anglian Water’s independently certified asset management plan filed with Ofwat. Other assets are depreciated evenly over their estimated economic lives, which are principally as follows:

Operational assets (30-80 years)

Buildings (30-60 years)

Fixed plant (12-40 years)

Vehicles, mobile plant and equipment (3-10 years)

For additional information, see Anglian Water’s 2005 Annual Report – Notes to the Financial Information – Note 1(c).

### ***Exceptional Items***

In the year ending 31 March 2003, Anglian Water incurred exceptional items relating to restructuring of its financing arrangements and reorganisation of the business. Anglian Water completed a process of restructuring its financing through the creation of the Anglian Water Services Financing Group (see Chapter 7, “*Financing Structure*”), which resulted in debt transfer costs, legal and advisers’ fees and bankers’ costs of £65.3 million for the year ended 31 March 2003. Reorganisation costs include staff redundancy costs, together with related unfunded early retirement pension obligations. Reorganisation costs incurred in the years ended 31 March 2004 and 2005 were not classified as exceptional costs.

### ***Consolidation***

Under the provisions of U.K. GAAP, Anglian Water is not required to prepare, and historically did not prepare, consolidated financial statements including the assets, liabilities, results of operations and cash flows of its subsidiary undertakings. Following the financial restructuring of Anglian Water completed on 30 July 2002, Anglian Water was required to produce consolidated financial statements pursuant to the Common Terms Agreement. Accordingly, the financial statements of Anglian Water for the years ended 31 March 2005, 2004 and 2003 have been prepared on a consolidated basis.

### ***Taxation***

For periods commencing after 1 April 2001, Anglian Water has adopted Financial Reporting Standard 19 (Deferred Taxation) (“**FRS 19**”) in relation to deferred taxes. FRS 19 requires full provision to be made for such deferred tax assets and liabilities that arise from timing differences between the recognition of gains and losses in the financial statements and their recognition in the tax computation. The deferred tax balances are discounted using the after tax yields to maturity on UK government bonds with similar maturity dates. Prior to adopting FRS 19, Anglian Water accounted for deferred taxation only to the extent that there was a reasonable probability that such deferred taxation would be payable in the foreseeable future. For additional information, see Anglian Water’s 2005 Annual Report – Notes to the Financial Information – Notes 1(k), 6 and 18.

### ***Regulatory Information***

In addition to its Statutory Accounts, as a condition of its Licence, Anglian Water, like all other Regulated Companies in England and Wales, is required to submit regulatory accounts to Ofwat in June of each year (the “**Regulatory Information**”) which comply with accounting conventions established by Ofwat. The Regulatory Information is to a certain extent used by the DGWS in establishing the five-year price cap for Anglian Water. Although Anglian Water’s Regulatory Information is included in its 2004 Annual Report and its 2005 Annual Report, potential investors should be aware that significant differences exist between the Regulatory Information and the Statutory Accounts. Anglian Water has made no attempt to identify or quantify the impact of those

differences. Unlike Anglian Water's Statutory Accounts, which are prepared under the historical cost convention, in its Regulatory Information, Anglian Water values assets relating to its water and sewerage operations at their current cost value to the business (with the exception of assets acquired prior to 31 March 1990 which are valued at the replacement cost equivalent of an asset with that operating capability). As a result, Anglian Water's recorded total tangible fixed assets at 31 March 2005 of £20,435.8 million in its Regulatory Information and £3,911.4 million in its Statutory Accounts. In addition to applying different valuation methods for tangible fixed assets, the Regulatory Information is based on different accounting policies with respect to grants and other third-party contributions. There is also a corresponding adjustment to depreciation. Furthermore, Anglian Water's Regulatory Information includes certain additional disclosures required by Ofwat. For additional information on the Regulatory Information, see Anglian Water's 2005 Annual Report – Regulatory Accounts and Required Regulatory Information and the related notes thereto.

## **Results of Operations**

### ***Year ended 31 March 2005 compared to year ended 31 March 2004***

*Turnover:* For the year ended 31 March 2005, Anglian Water's turnover increased by £30.2 million, or 3.9 per cent., to £796.8 million from £766.6 million in 2004. This increase was largely attributable to a £38.6 million increase in turnover due to the impact of the agreed price formula with DGWS (which permitted a price increase for services of 2.5 per cent. and an increase for inflation of 2.53 per cent. (resulting in an aggregate price increase of 5.03 per cent.)). Partially offsetting this increase was the impact of customers switching from unmetered to metered tariffs and higher than average revenues in 2003 due to the significantly lower than average rainfall in the summer months of that year.

*Operating costs before depreciation:* Operating costs before depreciation decreased by £0.6 million, or 0.2 per cent., to £291.1 million for the year ended 31 March 2005 from £291.7 million for the year ended 31 March 2004. The principal reasons for this decrease were efficiency savings following Group reorganisations in the two prior years being offset by inflation of £9.3 million and restructuring costs of £6.8 million in excess of the year ended 31 March 2004.

*Depreciation net of amortisation of grants and contributions:* Depreciation net of amortisation of grants and contributions increased by £10.4 million, or 6.7 per cent., to £166.4 million for the year ended 31 March 2005 from £156.0 million for the year ended 31 March 2004. This increase resulted from accelerated depreciation in the year of £3.4 million, primarily relating to IT assets, and higher levels of capital expenditure.

*Operating profit:* Operating profit was £339.3 million for the year ended 31 March 2005, an increase of £20.4 million, or 6.4 per cent., compared with operating profit of £318.9 million for the year ended 31 March 2004. Operating profit margin was higher at 42.6 per cent. for the year ended 31 March 2005 compared with 41.6 per cent. for the year ended 31 March 2004.

*Interest payable (net):* Interest payable (net) was £61.4 million for the year ended 31 March 2005, an increase of £11.7 million, or 23.5 per cent., compared with interest payable (net) of £49.7 million for the year ended 31 March 2004. The primary reason for this increase was an increase in the full year Retail Price Index leading to higher interest charges of £7.9 million on index linked debt. In addition, there was an acceleration of the write-off of issue costs of £1.9 million, relating to bonds that were called in July 2005.

*Tax on profit on ordinary activities:* Tax on profit on ordinary activities resulted in a charge of £12.4 million for the year ended 31 March 2005 compared with a credit of £33.5 million for the year ended 31 March 2004. In the year to 31 March 2004 there was a credit of £22.2 million in respect of previous periods' corporation tax due to the implementation of an agreement that Anglian Water would not pay for tax losses surrendered to it by Anglian Water Services Holdings Ltd as well as due to a credit resulting from the agreement of prior year tax computations. These credits did not recur for the year to 31 March 2005. In addition, the credit resulting from the discounting on deferred tax liability decreased by £22.1 million from 2004 to 2005. This lower credit resulted from changes in the ratio of the net book value of assets across asset classes between the two years and the effect of capital allowance disclaimers upon capital allowance pool tax written down values. Both factors affected the timing of the deferred tax provision reversal.

*Profit on ordinary activities after taxation for the financial year:* As a result of the foregoing factors, profit on ordinary activities after taxation for the financial year decreased by £37.2 million, or 12.3 per cent., to £265.5 million for the year ended 31 March 2005 compared with £302.7 million for the year ended 31 March 2004.

*Dividends paid/payable:* Dividends declared for the year ended 31 March 2005 were £253.1 million compared with £250.6 million for the year ended 31 March 2004. The dividends for the year ended 31 March 2005 consisted of £60.0 million declared to AWG Group Ltd and £193.1 million declared to Anglian Water Services Overseas Holdings Ltd, the immediate parent undertaking of Anglian Water. Anglian Water Services Overseas Holdings Ltd declared a dividend of £193.1 million to Anglian Water Services Holdings Ltd, the ultimate parent company of the Anglian Water Services Financing Group. The dividend was then used by Anglian Water Services Holdings Ltd to service interest payable on the intercompany loan provided under the Issuer/Anglian Water Loan Agreement by Anglian Water on 30 July 2002. See Section 7.4.2, “*Financial Structure – Intercompany Loan Arrangements – Issuer/Anglian Water Loan Agreements*”. This interest receivable is recorded in interest payable (net) in Anglian Water’s profit and loss account.

#### **Year ended 31 March 2004 compared to year ended 31 March 2003**

*Turnover:* For the year ended 31 March 2004, Anglian Water’s turnover increased by £39.8 million, or 5.5 per cent., to £766.6 million from £726.8 million in 2003. This increase is largely attributable to the impact of the agreed price formula with DGWS (which permitted a price increase for services of 2.5 per cent. and an increase for inflation of 2.65 per cent. (resulting in an aggregate price increase of 5.15 per cent.)) and, to a lesser extent, turnover generated by higher volumetric consumption during the significantly lower than average rainfall during the summer months in 2003 in the Anglian region. These increases were partly offset by the impact of customers switching from unmetered to metered tariffs.

*Operating costs before depreciation:* Operating costs before depreciation decreased by £9.4 million, or 3.1 per cent., to £291.7 million for the year ended 31 March 2004 from £301.1 million for the year ended 31 March 2003. This decrease was largely due to an exceptional operating cost of £18.6 million for the year ended 31 March 2003 relating to the Anglian Water financial restructuring programme completed on 30 July 2002 and redundancy costs. Without the exceptional operating costs in 2003, operating costs before depreciation would have increased by £9.2 million, or 3.3 per cent., from the year ended 31 March 2003 to the year ended 31 March 2004, in large part due to the inclusion of redundancy costs of £4.7 million within operating costs in 2004 and additional costs for the treatment and disposal of sludge.

*Depreciation net of amortisation of grants and contributions:* Depreciation net of amortisation of grants and contributions decreased by £0.9 million, or 0.6 per cent., to £156.0 million for the year ended 31 March 2004 from £156.9 million for the year ended 31 March 2003. This decrease was primarily due the full depreciation of some assets with comparably shorter lives in 2003.

*Operating profit:* Operating profit was £318.9 million for the year ended 31 March 2004, an increase of £50.1 million, or 18.6 per cent., compared with operating profit of £268.8 million for the year ended 31 March 2003. Operating profit margin was higher at 41.6 per cent. for the year ended 31 March 2004 compared with 37.0 per cent. for the year ended 31 March 2003.

*Interest payable (net):* Interest payable (net) was £49.7 million for the year ended 31 March 2004, a decrease of £56.1 million, or 53.0 per cent., compared with interest payable net of £105.8 million for the year ended 31 March 2003. Interest payable (net) for the year ended 31 March 2004 includes £193.6 million of interest receivable from Anglian Water Services Holdings Ltd in relation to an intercompany loan, an increase of £64.0 million from £129.6 million for the year end 31 March 2003.

Excluding this intercompany interest receivable and, in 2003, an exceptional interest charge of £49.6 million, the interest charge increased by £57.5 million, or 30.9 per cent., to £243.3 million for the year ended 31 March 2004 from £185.8 million for the year ended 31 March 2003. This increase reflects the fact that the 2003 charge includes the impact of the financial restructuring for only part of the year, whereas there is a full-year impact in 2004.

*Tax on profit on ordinary activities:* Tax on profit on ordinary activities resulted in a credit of £33.5 million for the year ended 31 March 2004 compared with a charge of £57.7 million for the year ended 31 March 2003. Of the total decrease, £57.1 million was due to the implementation of an agreement that Anglian Water would make no payment to Anglian Water Services Holdings Ltd for the tax losses surrendered to Anglian Water. In addition, there was a deferred tax credit of £27.2 million due to a year on year increase in the post-tax yields to maturity on government bonds which are used in the calculation of the discounted deferred tax provision.

*Profit on ordinary activities after taxation:* As a result of the foregoing factors, profit on ordinary activities after taxation increased by £193.5 million, or 177.2 per cent. to £302.7 million for the year ended 31 March 2004 compared with £109.2 million for the year ended 31 March 2003.

*Dividends:* Dividends declared for the year ended 31 March 2004 were £250.6 million, which represented a decrease of £38.0 million, or 13.2 per cent., from £288.6 million declared for the year ended 31 March 2003. The dividends for the year ended 31 March 2004 consisted of £57.0 million declared to AWG Group Ltd and £193.6 million declared to Anglian Water Services Overseas Holdings Ltd. Anglian Water Services Overseas Holdings Ltd declared a dividend of £193.6 million to Anglian Water Services Holdings Ltd. This dividend was used by Anglian Water Services Holdings Ltd to service interest payable on the intercompany loan provided by Anglian Water on 30 July 2002. This interest receivable is recorded in the net interest payable (net) of Anglian Water's profit and loss account.

### **Financial Condition**

In the balance sheet of the Statutory Accounts, Anglian Water's asset base consists of tangible assets and investments. Tangible assets consist mainly of the network infrastructure (such as the underground piping network for both the water supply and sewerage network) and non-network infrastructure (such as pumping stations, water treatment plants and sewage treatment plants).

Anglian Water accounts for supplies of materials used in the water and sewerage business (acquired in advance of requirements to ensure that the materials are readily available as and when required by the business) as stock. Such materials generally include infrastructure supplies such as replacement pipes, chemicals for water purification processes and mechanical and electrical hardware. The stock levels held by Anglian Water are relatively constant year-on-year.

Debtors for the most part consist of accounts receivable by Anglian Water. The predominant component of this line item in the Statutory Accounts is charges for use of the network (so-called "main charges") levied on customers (residential and commercial/large industrial). Other significant items included within debtors are amounts owed by Anglian Water Services Holdings Ltd to Anglian Water for interest receivable on the intercompany loan of £1,609.1 million provided on 30 July 2002 and pre-payments made to third-party vendors. Pre-payments comprise items such as the Ofwat licence fee (paid annually in advance), contract payments for laboratory services, laboratory rents and service payments to Anglian Water's IT contractor that are paid monthly in advance. Another component of this line item is VAT charges recoverable from the HM Revenue & Customs. Under applicable law, water and sewerage charges for residential customers are zero-rated for VAT purposes (residential customers do not pay VAT). Consequently, Anglian Water pays out more VAT than it receives in and can recover the net difference from HM Revenue & Customs.

Anglian Water accounts for portions of its loan portfolio that must be repaid in the next 12 months under short-term borrowings. Other creditors in respect of amounts falling due within one year ("other short-term creditors") consist principally of trade creditors in the ordinary course of business. Other components of short-term creditors include interest payable on borrowings, amounts paid in advance by unmetered customers and outstanding corporate taxes owed to the HM Revenue & Customs.

Anglian Water accounts for the portions of its loan portfolio that are repayable in periods beyond 12 months under loans and other borrowings. Other long-term creditors consist of grants and contributions received by Anglian Water principally from new housing developments in connection with extending necessary infrastructure and connections to Anglian Water's network. Anglian Water allocates such grants and contributions between infrastructure-related assets and non-infrastructure-related assets. Anglian Water includes amounts paid in respect of infrastructure-related assets (such as water mains) into Anglian Water's tangible assets. Anglian Water accounts for amounts in respect of non-infrastructure assets (such as water treatment facilities) under long-term creditors.

Provisions for liabilities and charges currently comprise three elements: (i) additional amounts in respect of certain unfunded supplementary pension obligations for employees that have been made redundant (as determined using actuarial assumptions based on those used for the valuation of the AWG Group's pension scheme); (ii) a provision which relates to coupon enhancement and other related costs incurred on the transfer of debt from the AWG Group to the Anglian Water Services Financing Group as part of the financial restructuring; and (iii) a provision for deferred taxation.

### ***As at 31 March 2005 compared to 31 March 2004***

*Tangible assets:* Tangible assets were £3,911.4 million as at 31 March 2005, an increase of £109.9 million, or 2.9 per cent., compared with tangible assets of £3,801.5 million, as at 31 March 2004. The increase is primarily due to capital expenditure of £293.7 million offset in part by the depreciation charge of £171.9 million and grants

and contributions amounting to £11.6 million from third parties towards expenditures related to infrastructure assets.

*Investments:* Investments were £1,609.2 million as at 31 March 2005 compared with £1,609.3 million as at 31 March 2004. Of this, £1,609.1 million represents a loan to Anglian Water Services Holdings Ltd made on 30 July 2002, the proceeds of which were used by Anglian Water Services Holdings Ltd to acquire Anglian Water Services Overseas Holdings Ltd and its subsidiary undertakings (which include Anglian Water) from AWG Group Ltd. The loan is repayable no earlier than 30 July 2038. Interest is calculated at 12.0 per cent. per annum and interest receivable of £193.1 million has been included in the profit and loss account for the year ended 31 March 2005.

*Debtors:* Debtors as at 31 March 2005 were £260.4 million, an increase of £7.4 million, or 2.9 per cent., compared to £253.0 million as at 31 March 2004. The increase was primarily due to an increase of £27.5 million in the value of the prepaid pensions contributions calculated in accordance with SSAP 24 "Accounting for Pension Costs" ("SSAP 24"), which was partially offset by a £13.7 million reduction in income not yet billed.

*Other short-term creditors:* Other short-term creditors were £382.4 million as at 31 March 2005, compared to £344.1 million as at 31 March 2004, an increase of £38.3 million, or 11.1 per cent. The increase is primarily due to an increase in the dividend payable creditor to other AWG Plc group undertakings of £19.5 million and an increase in receipts in advance of £10.6 million.

*Other long-term creditors:* Other long-term creditors were £98.4 million as at 31 March 2005, an increase of £8.4 million, or 9.3 per cent., compared to the £90.0 million as at 31 March 2004. This increase represents an increase in deferred income relating to grants and contributions received from developers for connecting new water and sewerage services.

*Provisions:* Provisions as at 31 March 2005 were £158.9 million, an increase of £9.9 million, or 6.6 per cent., compared to £149.0 million as at 31 March 2004. This increase was largely due to an increase of £10.6 million in the deferred tax provision due to a year on year increase in the post-tax yields to maturity on government bonds which are used in the calculation of the discounted deferred tax provision.

#### ***As at 31 March 2004 compared to 31 March 2003***

*Tangible assets:* Tangible assets were £3,801.5 million as at 31 March 2004, an increase of £104.8 million, or 2.8 per cent., compared to tangible fixed assets of £3,696.7 million as at 31 March 2003. The increase is primarily due to capital expenditure of £276.9 million offset by the depreciation charge of £161.9 million and grants and contributions from third parties towards expenditures related to infrastructure assets of £9.9 million.

*Investments:* There was no movement in the total of investments in the year and the balance as at 31 March 2004 remained at £1,609.3 million from 31 March 2003. Of this, £1,609.1 million represents the loan to Anglian Water Services Holdings Ltd made on 30 July 2002.

*Debtors:* Debtors as at 31 March 2004 were £253.0 million, a reduction of £11.2 million, or 4.2 per cent., compared to £264.2 million as at 31 March 2003. The main factor resulting in the reduction was a £22.6 million decrease in prepayments and accrued income primarily caused by some customer billing normally done in April being brought forward to March thereby reducing the amount accrued at 31 March 2004. This was offset by a £14.6 million increase in the value of the prepaid pension contributions calculated in accordance with SSAP 24.

*Other short-term creditors:* Other short-term creditors were £344.1 million as at 31 March 2004, compared to £449.7 million as at 31 March 2003, a reduction of £105.6 million, or 23.5 per cent. The reduction is almost entirely due to a reduction in the dividend payable to AWG Group Ltd of £94.5 million from £152.6 million at 31 March 2003 to £58.1 million at 31 March 2004. As at 31 March 2003 there was a final dividend of £70 million plus £35 million of an interim dividend unpaid compared to only £10 million unpaid at 31 March 2004.

*Other long-term creditors:* Other long-term creditors were £90.0 million as at 31 March 2004, an increase of £2.6 million, or 3.0 per cent., compared to the £87.4 million as at 31 March 2003. This increase represents an increase in deferred income relating to grants and contributions received from developers for connecting new water and sewerage services.

*Provisions:* Provisions as at 31 March 2004 were £149.0 million, a decrease of £15.0 million, or 9.1 per cent., compared to £164.0 million as at 31 March 2003. The decrease primarily resulted from a reduction of

£11.3 million in the deferred tax provision due to a year on year increase in the post-tax yields to maturity on government bonds which are used in the calculation of the discounted deferred tax provision.

### **Liquidity and Capital Resources**

For the years ended 31 March 2005, 2004 and 2003, net cash inflow from operating activities was £512.9 million, £484.0 million and £415.9 million, respectively. Included in net cash from operations are movements in Anglian Water's working capital. Working capital decreased by £38.1 million for the year ended 31 March 2005 and £26.6 million for the year ended 31 March 2004, and by £10.0 million for the year ended 2003.

Anglian Water had cash outflow of £25.3 million, £15.6 million and £64.6 million from returns on investments and servicing of finance in the years ended 31 March 2005, 2004 and 2003, respectively. The decreased cash outflow for the year ended 31 March 2004 was due to a reduction in net interest of £25.9 million comprising an increase in interest received of £111.0 million primarily due to approximately five months' interest received from Anglian Water Services Holdings Ltd relating to the intercompany loan for the year ended 31 March 2003 compared to twelve months' interest received for the year ending March 2004. This was partly offset by an increase of £85.1 million in interest payable due mainly to the timing of the initial interest payments being made in the current year relating to debt raised in July 2002. In addition, financing costs, which were £23.8 million for the year ended 31 March 2003 as a result of the refinancing undertaken in that year, decreased by £22.5 million to £1.3 million for the year ended 31 March 2004.

In relation to capital expenditure and financial investments, Anglian Water used cash (net of disposal proceeds) of £262.9 million in the year ended 31 March 2005, £256.9 million in the year ended 31 March 2004 and £1,543.0 million in the year ended 31 March 2003. Anglian Water's capital outlay consisted principally of investments in fixed assets of £290.9 million, £276.6 million and £261.7 million net of grant receipts of £26.9, £18.6 million and £17.0 million for the years ended 31 March 2005, 2004 and 2003, respectively. During the year ended 31 March 2003, as part of the refinancing completed on 30 July 2002, Anglian Water loaned £1,609.1 million to Anglian Water Services Holdings Ltd through an intercompany loan under the Issuer/Anglian Water Loan Agreement. This was partially off-set by the repayment of the £309.5 million loan made to AWG Group Ltd in the year ended 31 March 2002. During the year ended 31 March 2004 and 2005, no group company loans were issued or repaid.

In connection with acquisitions and disposals of investments, Anglian Water acquired £1.7 million of cash in the year ended 31 March 2003 through acquiring the trade and certain assets of Geodesys Ltd. No further acquisitions were made in the years ended 31 March 2004 and 31 March 2005.

The increase in short-term deposits to £503.4 million for the year ended 31 March 2005 from £180.8 million for the year ended 31 March 2004, which in turn represented an increase over short term deposits of £88.2 million for the year ended 31 March 2003, relates to cash invested in short-term money funds.

Net cash inflows from financing was £377.7 million, £428.1 million and £1,670.5 million for the years ended 31 March 2005, 2004 and 2003, respectively. The increase for the year ended 31 March 2005 includes proceeds of £398.3 million (net of issue costs) from the £250 million 5.25% bond and £150 million 5.5% bond issued by the Issuer less £17.3 million of finance lease repayments.

Overall, there was a net decrease in cash of £135.3 million in the year ended 31 March 2005, compared to a net increase in cash of £114.0 million in the year ended 31 March 2004 and an increase of £256.8 million in the year ended 31 March 2003.

At 31 March 2005, net debt was £3,499.4 million (£4,251.1 million in long-term borrowings, £88.1 million in short-term borrowings and £839.8 million of cash and short-term deposits), an increase of £48.5 million over net debt of £3,450.9 million at 31 March 2004 (£3,900.6 million in long-term borrowings, £22.0 million in short-term borrowings and £471.7 million of cash and short-term deposits), which in turn was an increase of £161.5 million over net debt at 31 March 2003 of £3,289.4 million (£3,438.9 million in long-term borrowings, £27.4 million in short-term borrowings and £176.9 million in cash).

Long-term borrowings increased at 31 March 2005 compared to 31 March 2004 by £350.5 million principally due to the proceeds of a €650.0 million bond issue (£453.2 million). Long-term borrowings increased at 31 March 2004 compared to 31 March 2003 by £461.7 million due principally to the proceeds of a €650.0 million bond issue (£453.2 million).



Short-term borrowings were £88.1 million at 31 March 2005, increased from £22.0 million compared to 31 March 2004. Short-term borrowings were £22.0 million at 31 March 2004, a reduction of £5.4 million or 19.7 per cent. compared to £27.4 million at 31 March 2003. The decrease results from the timing of repayments on finance leases.

Cash and short-term deposits were £839.8 million, £471.7 million and £176.9 million at 31 March 2005, 2004 and 2003, respectively. The 31 March 2005 balance comprises £214.4 million of prefunding for capital expenditure, £206.9 million for working capital and £418.5 million for debt servicing. The increase between 31 March 2003 and 2004 is principally due to £453.2 million in proceeds from a new bond issue less dividends paid to AWG Group Ltd of £152 million.

### **Capital Expenditure**

The capital expenditure figures set forth below are not derived from the Cash Flow Data set forth in “*Cash Flow Data*” above. They represent accounting expenditures including accruals for the periods or years indicated.

Capital expenditure was £293.7 million, £276.9 million and £263.3 million for the years ended 31 March 2005, 2004 and 2003, respectively, and represented the final three years of Anglian Water’s five-year asset management plan agreed with the DGWS (“AMP3”). Approximately £98.7 million, £85.7 million and £94.9 million was expended on water infrastructure during the years ended 31 March 2005, 2004 and 2003, respectively, while a further £195.0 million, £191.2 million and £168.4 million was expended across a wide range of individual assets relating to sewerage infrastructure during these respective periods.

The price review allowed approximately £1.6 billion for the five years ending 31 March 2005 for improvements to maintain serviceability, meet new demand and further improve the quality of drinking water, bathing and river water. Since 1 April 2000, the start of the five-year AMP3 period, investment totalled £1.4 billion. Cumulative spend was below determination expectations which was attributed to the achievement of efficiencies in the Capital Programme and an under spend of £120 million on sludge incinerators which has been logged down from RCV on 1 April 2005.

## CHAPTER 4

### ANGLIAN WATER BUSINESS DESCRIPTION

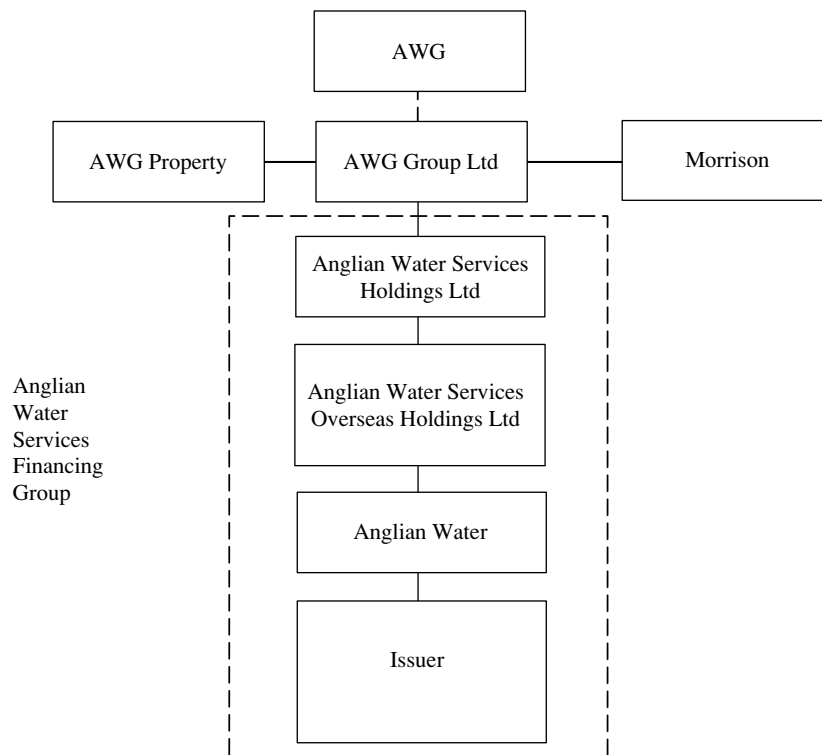
#### The AWG Group

AWG plc (“**AWG**”) is the ultimate holding company for the AWG Group, the principal business of which is Anglian Water, the group’s regulated water and wastewater company. The group also includes Morrison, a support services and construction business and AWG property, a property development business. The shares of AWG are admitted to the Official List and traded on the London Stock Exchange. As at September 2005, AWG had an equity market capitalisation of approximately £1,394.6 million. AWG’s wholly-owned subsidiary, Anglian Water Services Limited (“**Anglian Water**” or the “**Company**”), operates the AWG Group’s regulated water and sewerage business in England. In the year ended 31 March 2005, the AWG Group had total assets less current liabilities of £5,073.7 million, recorded net turnover of £1,796.9 million and employed 10,549 people.

AWG has created three distinct areas within its existing corporate structure, each with its own objectives and financing structures: a regulated water and sewerage business in England and Wales, operated by Anglian Water; a support services and construction business (“**Morrison**”) which builds and maintains public infrastructure through private financing, construction and support services divisions, and a property development business (“**AWG Property**”).

To maintain Anglian Water’s position as one of the leading water and sewerage companies in England and Wales, AWG restructured Anglian Water within the AWG Group in 2002 by establishing a “ring-fenced” financing group to separate (so far as practicable) Anglian Water financially and operationally from the rest of the AWG Group. AWG’s management believes that the ring-fencing structure provides significant benefits to Anglian Water, providing better access to the long term debt markets and an opportunity to reduce significantly the cost of capital employed in the regulated business, thereby enhancing shareholder returns. AWG believes that the ring-fencing structure also provides the best operating environment to sharpen management focus in the regulated water supply and sewerage business and align incentives. See Chapter 5, “*Ring-fencing and the Anglian Water Services Financing Group*”.

Set out below is the structure of the AWG Group, as of the date hereof:



## **Anglian Water**

### ***Overview***

Anglian Water serves the largest geographic area of the regional water and sewerage companies in England and Wales, covering an area that stretches from the Humber bank in the North to the Thames estuary in the South and from Daventry in Northamptonshire to the East Coast. It also includes the town of Hartlepool in the Northeast of England. Anglian Water provides water services to approximately 4.2 million people in an area covering approximately 22,000 square kilometres and sewerage services to approximately 5.9 million people in an area covering approximately 27,500 square kilometres. Based on the latest published Ofwat financial performance and expenditure report (relating to 2003-04), Anglian Water is the fourth largest of the ten regulated water supply and sewerage companies in England and Wales in terms of its regulatory asset value. In addition, on the basis of regulatory accounts which Anglian Water files with Ofwat (the “**Regulatory Information**”), for the year ended 31 March 2005, Anglian Water’s appointed water and sewerage activities generated turnover of £789.6 million and its net cash inflow from water and sewerage activities was £533.7 million. See Anglian Water’s 2005 Annual Report – Regulatory Accounts and Required Regulatory Information.

The region in which Anglian Water operates is mainly rural and agricultural but also includes several urban centres such as Cambridge (sewerage only), Peterborough, Norwich, Lincoln, Milton Keynes, Ipswich, Hartlepool and Grimsby. Because of the historical development of water supply and sewerage services in Anglian Water’s region, there are a number of areas (mostly in the south), such as Cambridge, Chelmsford and Basildon where Anglian Water provides sewerage services only and local water companies provide water services. Anglian Water has also gained four “inset” appointments to operate water services in areas outside its principal water supply licence area. For more information relating to “inset” appointments, water supply licensing and initiatives by the UK government to promote competition in the water and sewerage industry in England and Wales, see Chapter 11, “*Regulation of the Water and Sewerage Industry in England and Wales – Competition in the Water Industry*”. Within Anglian Water’s water supply and sewerage licence areas, there are a number of significant industrial customers in the petroleum, electricity and food processing sectors. The region in East Anglia where Anglian Water principally operates has had population growth of approximately 0.5 per cent. per year between 1996 and 2005. Anglian Water’s water supply and sewerage licence areas within East Anglia are part of the driest regions in the UK. Consequently, Anglian Water has invested considerable resources in developing reservoirs and supply management technology to deal with more limited water supplies.

### ***History***

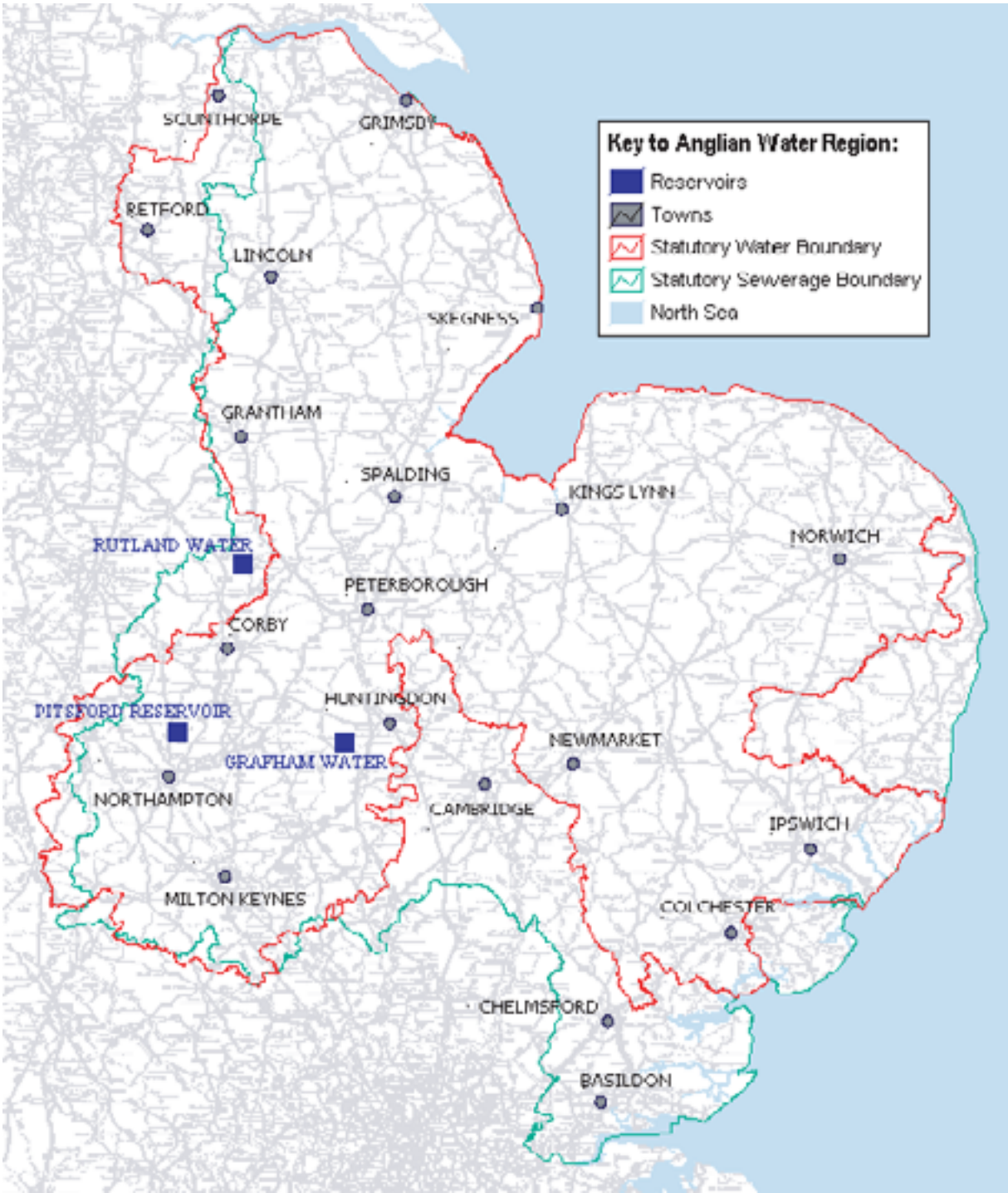
Anglian Water is a limited company registered under the Companies Act under number 2366656, and is a subsidiary of AWG. Anglian Water was appointed by an Instrument of Appointment dated 24 August 1989 (with effect from 1 September 1989) by the then Secretary of State for the Environment, as a Regulated Company under the provisions of Sections 11 and 14 of the Water Act 1989 (now replaced by Sections 6 and 11 of the Water Industry Act 1991 (“**WIA**”)) for a wide area of Eastern England and the Midlands. Before 1 September 1989, the former Anglian Water Authority provided water and sewerage services in those areas. In 1997, AWG Group Ltd acquired Hartlepool Water plc. On 1 April 2000, the appointment of Hartlepool Water plc as a water undertaker was merged with that of Anglian Water.

### ***Regulation and Licence***

Anglian Water operates within a highly regulated industry in England and Wales and its operations are strongly influenced by economic, drinking water quality and environmental regulation. Anglian Water is licensed to operate as a Regulated Company in England and Wales. In particular, Anglian Water’s business and results are affected by the regulated tariff rates which Anglian Water may charge its customers as approved by the DGWS as well as by drinking water quality and environmental regulations and the terms of its Licence. Every five years, the DGWS sets a price cap intended to enable water and sewerage companies in England and Wales to finance their operations and earn a reasonable return on capital. The final determination of the limits for 2005-10 was published on 2 December 2004. From 2006, the WSRA is expected to undertake the DGWS’s price-setting function. See Chapter 3, “*Management’s Discussion and Analysis of Financial Condition and Results of Operations*”, Chapter 6, “*Risk Factors*”, Chapter 11, “*Regulation of the Water and Sewerage Industry in England and Wales*” and Chapter 12, “*Modifications made to Anglian Water’s Licence*”.

Each year, Anglian Water’s systems for planning and internal controls as well as regulatory information prepared by Anglian Water are subject to review by Ofwat. This review function will also be undertaken by the WSRA. All water balance, leakage and drought-related data specified for 2005 have not yet been verified by Ofwat.

Set out below is a map of Anglian Water’s water supply and sewerage licence areas as at privatisation in 1989. The water supply licence area now includes the town of Hartlepool and three inset appointments: (i) at 2 Sisters Premier Division (formerly Buxted Chicken) in Flixton, Suffolk and (ii)-(iii) at Wynyard Park and Wynyard South, near Wolviston in Cleveland. The sewerage licence area now includes one inset appointment at RAF Finningley in South Yorkshire.



## ***Strategy***

Anglian Water's aspiration is to be "Leading our industry; taking pride in what we do; vital to the communities we serve":

- |         |  |
|---------|--|
| Leading | Whilst ensuring we run our business effectively, we will focus on leading in the areas of: <ul style="list-style-type: none"><li>● Capital and operating expenditure efficiency, so that we will become a frontier company;</li><li>● Supplier of choice with our business and developer customers, as we aim to never lose customers to competition;</li><li>● Supply/demand balance, driving the agenda on long-term water resources in the east of England;</li></ul>   |
| Vital   | With our stakeholders and within our communities, we will focus on: <ul style="list-style-type: none"><li>● Maintaining the highest possible safety and public health standards – demonstrating the leading practice in the industry;</li><li>● Driving the customer experience through our service principles, so that our customers and key stakeholders see us as leading in our service provision;</li><li>● Contributing to the prosperity and sustainability of the region through our management of natural resources, through our role as an employer, and through the provision of service;</li></ul> |
| Proud   | We will become leading through our people, because: <ul style="list-style-type: none"><li>● We continuously develop our staff within our skills and behaviours framework;</li><li>● Our employees are proud to work for Anglian Water;</li><li>● We share and celebrate our successes.</li></ul>   |

## ***Water Supply Services***

Anglian Water's water supply services to customers consist of the "abstraction" of water and its subsequent treatment and distribution to homes and other premises. Abstraction refers to the removal of water from surface sources, such as reservoirs and rivers, or from underground sources, such as aquifers. Water requires treatment before it can be supplied for domestic purposes. Untreated or partially treated water, however, may be supplied, principally for industrial or agricultural use. The extent of treatment depends on the nature of the source, the quality of the untreated water and its intended use. Water abstracted from rivers requires extensive treatment but water drawn from groundwater sources usually requires less treatment. For surface water, the treatment involves several phases, including coagulation (which involves adding iron salts to the water), sedimentation, filtration and, if necessary, more sophisticated treatment such as exposure to ozone and granular activated carbon before the final phase of disinfection with chlorine. Water is distributed through networks of interconnected mains, service reservoirs and water towers.

## ***Water Resources and Supply***

Of the water abstracted by Anglian Water for public supply in its licensed water region, approximately 50 per cent. consists of groundwater abstracted from aquifers, approximately 45 per cent. is abstracted from large raw water storage reservoirs which are refilled by abstraction from rivers, and approximately 5 per cent. is abstracted directly to water treatment works from rivers. Anglian Water holds abstraction licences for seven aquifers and operates seven reservoirs, of which the five major reservoirs have 208 million cubic metres of storage capacity.

The mix of water supply resources in the Anglian Water licence area is largely a product of historical development and geology. The region in which Anglian Water operates is underlain by chalk, limestone and sandstone strata which readily absorb and release rainwater and are suitable for cost effective bore-hole drilling. In addition, other factors which contribute to Anglian Water's current mix of water supplies are water quality, environmental and cost considerations. Aquifers and reservoirs provide more reliable water supplies than direct river abstraction as rainwater can be stored from the winter to maintain supplies during summers and to provide security against drought.

The three largest surface water storage reservoirs of Anglian Water, Rutland Water, Grafham Water and Pitsford Water, are linked through trunk supply mains to form the “Ruthamford” system. This facilitates water management in periods of low rainfall for the major urban areas in the west of Anglian Water’s licence area where growth is highest. In addition, Anglian Water relies on water demand modelling to maintain a secure balance of water supply and demand. The demand for water is forecast by considering the components of residential and commercial/industrial supplies and leakage. This is supported by extensive analysis of domestic water use, economic analysis of trends in industrial demand and the evaluation of the economic levels of leakage. The forecasts are revised periodically and agreed with Ofwat and the EA. Forecasts of demand include the distribution and predicted growth of population at local level and the impact of climate on the peak demand for water. While there is generally little significant seasonal fluctuation in the total water put into supply, the quantity of treated water supplies varies during the year and fluctuations are due to a variety of factors, such as dry weather and burst pipes due to freeze/thaw cycles affecting the ground during winter months.

Anglian Water monitors volumes of abstracted water from the environment through a fully maintained and telemetered metering system. Over 300 meters are affixed to all abstraction points. The telemetered flow data from these meters is recorded on the Licensed Abstraction Reporting System (LARS). Similarly all treated water leaving Anglian Water’s 150 treatment works is measured through a fully maintained and telemetered system. Over 200 meters are affixed to all treatment works outputs. The telemetered flow data from these meters is recorded on the Source Works Output Reporting System (SWORPS).

Anglian Water is recognised as an industry leader in the field of leakage control. Although it serves the largest geographic area in England and Wales, in 2004-05 Anglian Water achieved its Economic Level of Leakage (“ELL”) target of 216.7 megalitres per day (“ML/d”) achieving an average leakage performance of 214 ML/d for the year. This performance represents a leakage level of 6m<sup>3</sup>/km/day which is one of the lowest in England and Wales with a reported industry average of 11m<sup>3</sup>/km/day. This performance is the result of Anglian Water’s sustained investment in leakage control technology and its significant water infrastructure renewal strategy. Anglian Water has over 2,500 distribution and district meters, which are flow measuring devices affixed to points along the water mains that measure water delivery to each of Anglian Water’s distribution zones and district metered areas. These meters are connected to the telemetry system which enables Anglian Water to quickly identify increased water flows into areas and investigate any associated increase in leakage.

As a consequence of its reliable water resources, integrated strategic network, water demand management capabilities and industry leading leakage position, Anglian Water has been able to avoid imposing any restrictions on water usage since 1991, when the use of hosepipes for garden watering was banned in part of Anglian Water’s water supply licence area for the whole of that summer.

#### *Customers and Turnover*

During the year ended 31 March 2005, Anglian Water supplied an average of 1,163 megalitres of treated water and 48 megalitres of untreated or partially treated water per day to approximately 1.96 million properties in the Anglian Water licence area. In addition, in the same period, Anglian Water installed approximately 18,000 new water connections. Anglian Water’s customer base for water services is predominantly residential, accounting for approximately 66 per cent. of Anglian Water’s delivered volume. Commercial and large industrial customers represented the balance of Anglian Water’s delivered volume.

Anglian Water has around 200 industrial customers who use more than 50 megalitres per year. However, no single customer accounts for more than 0.63 per cent. of Anglian Water’s revenues from its water services operations. On the basis of the Regulatory Information for the year ended 31 March 2005, turnover from the water business for that year was £309.6 million and comprised 39.2 per cent. of Anglian Water’s turnover (relating to Anglian Water’s Regulated Business).

#### *Water Services Infrastructure*

Anglian Water operates 144 water treatment plants, producing over 1.1 billion litres of water a day, and maintains 36,860 km of water mains. Around 30% per cent of the water mains are made of iron, 25% are made of high-density polyethylene pipe, 17% are PVC, and the remainder a variety of other materials. To meet regulatory guidelines concerning water quality, Anglian Water rehabilitated over 3,000 km of iron mains between 1995 and 2003. This programme involved replacing the old iron mains with new polyethylene pipes or scraping and relining the interior of the old mains. This investment has helped to further reduce leakage and the susceptibility of mains bursts; the leakage performance is one of the best of the water and sewerage companies in the UK.

### *Capital Investment*

Between 1 April 2000 and 31 March 2005, Anglian Water invested £479 million in capital projects related to improvements in water treatment and water delivery infrastructure, of which £212 million was invested in new assets and £267 million was invested in maintaining existing infrastructure.

The principal investment targets related to Anglian Water's water services under the capital investment programme included: £109 million for maintenance of water treatment works, reservoirs and water pumping stations; £102 million for maintenance related to water mains, £126 million for investment in installing new meters and related expenditures for new water customers; and £84 million for improved drinking water quality.

### *Drinking Water Quality and Service Performance*

To assess compliance with drinking water standards established in the Water Quality Regulations, Anglian Water monitors water quality through an extensive programme of regular sampling and analysis. The Water Quality Regulations require that samples must be taken depending on the volume produced or the population served. In addition, all service reservoirs must be sampled weekly. Regulatory analysis is also carried out at water treatment works and service reservoirs to ensure that water has been adequately disinfected and is safe to drink.

Detailed analysis is made from samples taken at the point of consumption (i.e., the customer's tap). This analysis includes all chemical and bacteriological parameters prescribed by the Water Quality Regulations. The frequency with which samples are taken and the analysis made depends on population size. Results of analysis falling outside the prescribed parameters are investigated and reported on a monthly basis to the DWI, which has the power to require improvements or take other enforcement action, although it may refrain from doing so if satisfied that Anglian Water is taking appropriate remedial action.

As a consequence of Anglian Water's continued investment and quality control in drinking water quality, in 2003, the DWI included Anglian Water with one other water company categorised as significantly above average in the Overall Quality Index for England and Wales in the Report, "Drinking Water 2003" of the Chief Inspector of Drinking Water.

Anglian Water's performance is reported to Ofwat in an annual return each June. Historically, this includes reporting the water balance, leakage and drought-related measures such as sufficiency of supply and restrictions on water use, none of which has had a significant impact on water supplies to Anglian Water customers in the last 10 years. Comparative performance is reflected in Ofwat's overall performance assessment, which includes all service related measures.

### *Ofwat measures*

There are separate reports for operational measures of pressure and interruptions to supply that can affect customers, reported to Ofwat as DG2 and DG3 respectively. DG2 is "properties at risk of experiencing low water pressure" and DG3 is "properties experiencing unplanned supply interruptions". For 2004/05 Anglian Water has reported performance below the industry average for both measures, subject to verification by Ofwat.

With respect to its DG2 rating, Anglian Water's management believes that the extensive reach of Anglian Water's network, coupled with the largely flat geography in East Anglia, have contributed to its relative performance. However, since privatisation in 1989, the number of properties on Anglian Water's DG2 register has fallen from nearly 40,000 in 1991 to around 1,049 in 2005 as a result of targeted investment, including the installation of booster pumping stations. Anglian Water has not allocated any funding to reduce pressure problems, although some improvements have arisen as a consequence of the extensive investment in rehabilitating water mains during the previous price-review period.

Anglian Water's DG3 performance score (an index of the number of properties affected by unplanned supply interruptions as a percentage of the total properties connected to water) deteriorated from 0.65 for 2003-04 to 1.06 for 2004-05.

### *Wastewater Services*

Anglian Water's wastewater services consist of the collection and disposal of sewage including domestic sewage, trade effluent and surface water (including highway drainage). Wastewater is collected through networks of 35,770 km sewers via 4,440 pumping stations and treated at sewage treatment works, aside from that discharged through a single remaining long sea outfall. The organic waste is treated, dried and used in agriculture as a natural fertiliser.

### *Customers and Turnover*

For the year ended 31 March 2005, Anglian Water received an estimated flow of 946 megalitres per day of sewage into its sewerage network, which covers approximately 2.49 million properties. This included an average volume of 75 megalitres per day of trade effluent from approximately 2,500 industrial customers. During the year ended 31 March 2005, Anglian Water installed approximately 24,000 new sewerage connections (which includes approximately 18,000 new connections within Anglian Water's water supply licence area and approximately 6,000 outside its water supply licence area). Ninety-five per cent. of Anglian Water's customers are residential and 5 per cent. are industrial/commercial customers. Currently, no single customer accounts for more than 0.23 per cent. of Anglian Water's total revenues from sewerage services. On the basis of the Regulatory Information for the year ended 31 March 2005, turnover from the sewerage business for that year was £479.9 million or 60.8 per cent. of Anglian Water's turnover (relating to Anglian Water's Regulated Business).

### *Capital Investment*

Between 1 April 2000 and 31 March 2005, Anglian Water had invested approximately £882 million in capital projects related to improvements in sewerage treatment and sewerage infrastructure, of which approximately £493 million was for investment in new assets and £389 million was invested in maintaining existing infrastructure. Specifically, Anglian Water has continued to make significant investments to ensure that its sewage treatment plants are able to comply with discharge standards determined by the EA.

The principal investment targets related to Anglian Water's sewerage operations under the capital investment programme included: £400 million towards environmental improvement projects related to Anglian Water's sewerage operations; £209 million for maintenance of sewage treatment works and sewage pumping stations; £97 million for maintenance related to sewers; and £93 million for infrastructure and related expenditures for new sewerage customers.

### *Pollution and Quality Control*

Sewage is collected via Anglian Water's sewerage networks and treated at its sewage treatment works. The effluent from sewage treatment works is discharged to controlled waters (including most rivers and other inland and coastal waters) in accordance with consents issued and regulated by the EA. Another product of sewage treatment is sewage sludge. Approximately 86.3 per cent. of sewage sludge (bio-solids) processed by Anglian Water is recycled to agricultural land, approximately 6.4 per cent. is used in land reclamation and the remainder of the sludge that is unsuitable for recycling to agricultural land is disposed of in landfill sites. The management of sludge produced at sewage treatment works is strictly controlled. Disposal to landfill sites is becoming increasingly restricted due to tightening legislation and reducing landfill space. In addition, all sludge disposed of in this way is subject to a landfill tax. The recycling of treated sludge to agricultural land is controlled by UK regulations, compliance with which is monitored by the EA.

As a result of Anglian Water's continued investment in sewage treatment works, as at December 2004, 99.79 per cent. of Anglian Water's customers were served by sewage treatment works that complied with their regulatory look-up tables, which are used to assess sewage treatment works compliance. See Chapter 11, "*Regulation of the Water and Sewerage Industry in England and Wales – Principal EU Law*".

Ofwat has now excluded bathing water compliance from the basket of measures it uses to assess water company performance ("**Operational Performance Assessment**"). Ofwat has replaced the bathing water measure with the level of compliance of Anglian Water's ultra-violet ("**UV**") disinfection plants. All of Anglian Water's six consented UV plants were compliant in 2003.

Anglian Water seeks to ensure high levels of bathing water quality. Bathing water quality in 2004 was of an extremely high standard, with 100 per cent. compliance with the mandatory coliform standards of the Bathing Water Directive in 2004. This is the sixth season out of the last eight that Anglian Water has maintained this record. This is the best track record of any water company in England and Wales with a coastline.

Beaches within Anglian Water's region were awarded 18 Blue Flags in 2005, the same as in 2004. Blue Flags are awarded annually to beaches that meet guideline standards under the Bathing Water Directive and 25 beach management criteria. Anglian Water's region provided 25 per cent. of the Blue Flags in England although it covers just 10 per cent. of the beaches, and it has the highest concentration of Blue Flags amongst all the water companies in England and Wales.

This improving trend over the last ten years demonstrates Anglian Water's commitment to the implementation of its Blue Flag Water Policy ("**Blue Flag Water Policy**") – which aims for 100 per cent.



compliance with both the mandatory and guideline coliform standards by 2005. Full compliance with the guideline coliform standard however requires actions by third parties to mitigate the effects of discharges not within Anglian Water's control.

### ***Customer Charges***

Charges for water supply and sewerage services are calculated separately based on the average costs of providing each service for each class of customer. Customers with unmetered supplies are billed primarily in advance on an annual basis with payment being annually, half-yearly or by instalments. For supplies of metered water, non-domestic customers are billed periodically depending on the size of their consumption and domestic customers are normally billed half-yearly, in all cases in arrears. See Chapter 3, "*Management's Discussion and Analysis of Financial Condition and Results of Operations – Turnover*".

Charges for bulk supplies of water are usually determined on an individual basis, as are charges for some larger commercial water supplies and some industrial sewerage. The charging basis for bulk supplies in some cases provides for annual recalculation by reference to the expenditure associated with the supply. Trade effluent from industrial users is normally charged on a formula basis taking account of the volume of sewage, its strength and costs of removal and treatment.

According to forecast data compiled by Ofwat, the average annual household bill within the water supply and sewerage licence areas served by Anglian Water for the year ended 31 March 2006 will be £304, comprising £134 for water supply and £170 for sewerage services. The DGWS sets limits on the charges Anglian Water may levy for its water supply and sewerage services, including the amount of annual weighted average charge increases. On 2 December 2004, the DGWS published his final determination of price limits for the period 2005-2010. These price limits will result in an average increase of 2.4% per year for Anglian Water customers before adjustment for inflation. The DGWS will permit Anglian Water price increases of 3.8% in 2005-2006, 0.0% in 2006-2007, 2.8% in 2007-2008, 2.7% in 2008-2009 and 2.7% in 2009-2010. See Chapter 3, "*Management's Discussion and Analysis of Financial Condition and Results of Operations*", Chapter 6, "*Risk Factors*" and Chapter 11, "*Regulation of the Water and Sewerage Industry in England and Wales*".

Anglian Water has the highest proportion of metered customers among the water and sewerage companies in England and Wales (currently approximately 54 per cent. of Anglian Water's residential customers are metered compared to approximately 26 per cent. of residential customers throughout England and Wales, for the year ended 31 March 2005). Although the domestic rating system was discontinued in 1990 (under the provisions of the UK Local Government Finance Act 1988), under the WIA, water companies were originally allowed to continue to use rateable values for charging until 1 April 2000. More recently, following a review of water and sewerage charges in England and Wales, the UK Government has allowed companies to continue using the system after that date. At the same time it has made changes designed to encourage the use of water meters on domestic properties. See Chapter 3, "*Management's Discussion and Analysis of Financial Condition and Results of Operations*" and Chapter 11, "*Regulation of the Water and Sewerage Industry in England and Wales*".

As a consequence of the experience gained in respect of metering, Anglian Water has developed and introduced a number of tariff options, one of which, the Solow or low-user tariff, is believed to be the most popular optional tariff in the water industry. In 1998, Anglian Water was the first regulated water and sewerage company in England and Wales to introduce a tariff which targeted assistance at the more vulnerable customer groups. This idea was later adopted by the UK Government and, under regulations made under the WIA, it is now mandatory for all water and sewerage companies in England to offer a tariff to assist certain vulnerable customer groups.

In the last few years, Anglian Water has expanded the range of tariffs available to non-residential customers with the result that charges more closely reflect the costs of servicing the different types and sizes of customers. Management believes this development makes charges fairer to customers by providing customers with more choices.

Anglian Water offers a range of separate tariffs to industrial customers. Its range of large user tariffs now covers drinking water, sewerage, and trade effluent. Further refinements include separate tariffs for non-potable water, and the availability of an interruptible tariff. These are augmented by a change in the structure of tariffs for large water users, whereby the maximum daily water demand of each customer is subject to a separate and increasingly significant charge. These customers bills are therefore based not only on the volume of water they use, but on their peak usage profiles.

### *Bad Debts*

Following the introduction of the WIA in 1999, regulated water and sewerage companies were barred from disconnecting residential customers from their water supply for failure to pay bills. Industrial and commercial customers, however, are subject to a number of actions, including disconnection where persistent failure to settle charges occurs. Anglian Water, through the use of a dedicated billing call centre, contacts customers who are in arrears and arranges payment plans wherever possible. Bad debts are measured by Anglian Water as a percentage of Anglian Water's gross turnover (as reported in the Regulatory Information). In the year ended 31 March 2005, Anglian Water's bad debt ratio was 1.74 per cent., compared to the most recently published industry average in England and Wales of 2.15 per cent. in 2004-05.

### *Suppliers*

Anglian Water relies on a number of key inputs to operate its water and sewerage services which a number of international, UK and intra-AWG Group companies provide. Anglian Water relies on (i) IT software and hardware to monitor delivery to and supply from its water and sewerage network and billing of customers, (ii) electricity to operate pumping stations, treatment plants and the pipe network, (iii) chemicals for water purification and sewage treatment and (iv) a variety of materials as well as logistics and support services relating to construction of plants, installation of network infrastructure and other capital plant work. Procurement activities have now concluded for successor contracts for the development and maintenance of Anglian Water IT services. After an extensive sourcing process, the new contracts have both been awarded to the incumbent contractor. In respect of electricity costs Anglian Water, like similar companies, has experienced significant increases in recent years, which it mitigates by monitoring prices and tendering on the open market.

### *Outsourcing*

Like most of its competitors in the water and sewerage industry, Anglian Water outsources the majority of its capital investment programme and many of its day-to-day operations to third-party providers of goods and services. Over 70 per cent. of Anglian Water's capital investment programme is carried out by strategic design and construction partners who are monitored through a number of key performance indicators. The outsourced operations include water pipe repair and maintenance, IT services, training services, facilities management, logistics functions and some minor operations such as certain sewerage contracts.

The Common Terms Agreement sets out parameters that Anglian Water must adhere to in connection with its outsourcing of contracts. See Chapter 7, "*Financing Structure*".

The DGWS has imposed extensive requirements on Anglian Water to act properly and to report in respect of its outsourcing policy. However, the DGWS has agreed that Anglian Water is not required to submit a Procurement Plan as long as outsourcing levels are maintained at their current position. See Chapter 12, "*Modifications made to Anglian Water's Licence*".

### *Dividends and Dividend Policy*

For the period to 31 March 2010 Anglian Water intends to distribute substantially all cash inflow from operating activities after net interest payments and capital maintenance expenditure (based on allowances for current cost depreciation and infrastructure renewals charge given by Ofwat at the 2004 Price Review) to Anglian Water's shareholders by way of dividend subject to the covenants set out in the CTA and the availability of distributable reserves. For the year ended 31 March 2005, Anglian Water declared a dividend of £60.0 million payable to AWG Group Ltd. In addition, for the year ended 31 March 2005, Anglian Water declared a dividend of £193.1 million which will ultimately be used to service interest payable on an intercompany loan provided by Anglian Water to Anglian Water Services Holdings Ltd. See Section 7.5, "*Financing Structure – Common Terms Agreement*" and Chapter 3, "*Management's Discussion and Analysis of Financial Condition and Results of Operations – Results of Operations – Year ended 31 March 2005 compared to year ended 31 March 2004*".

### *Insurance and Risk Management*

Anglian Water maintains insurance coverage consistent with the principles of Good Industry Practice. This insurance is maintained as part of the AWG Group insurance programme. Anglian Water has procured a number of insurance policies, as set out in Schedule 16 of the CTA. These have been reviewed and approved by an independent insurance adviser retained to ensure that Anglian Water's insurances (i) are consistent with Good Industry Practice, (ii) have regard to the risk being covered and (iii) address the interests of Anglian Water and each finance party.

The insurance strategy for Anglian Water has been to tailor its insurance cover to address various aspects of Anglian Water's risk profile as well as develop robust risk management systems. With respect to high severity but low probability (catastrophic) events that management believes would significantly impact Anglian Water's business (such as a dam burst), the risk management policy has been to purchase insurance from external carriers.

With respect to medium severity but medium probability events (such as fire and flooding), Anglian Water has pursued a mix of options designed to accomplish cost effective coverage of Anglian Water risks, including purchasing insurance coverage from external carriers and self-financing from a dedicated insurance fund managed by the treasury department of Anglian Water. With respect to low severity but high probability events, management generally does not view it as cost effective to purchase insurance products for these relatively predictable losses and Anglian Water makes provision for such losses and liabilities from either the dedicated insurance fund or from operating profit.

As part of its strategy to ensure effective insurance, Anglian Water's policy is to use only external insurance providers approved by Willis Limited's Insurance Committee or any such other reputable insurance broker appointed in the future, who monitor and advise the AWG Group's insurance department of any deterioration in the credit rating of Anglian Water's insurance carriers.

Anglian Water has various risk control processes in place that management believes effectively monitor operational risks. For example, it has a rolling inspection programme for mechanical and electrical equipment. Structural engineers review the condition of dams and other infrastructure. Anglian Water works closely with UK Government departments to ensure that key installations are fully protected and the most significant unmanned premises are monitored by telemetry systems. Moreover, Anglian Water constantly monitors water quality.

The Common Terms Agreement contains provisions requiring Anglian Water's on-going insurance regime to meet various criteria. These are outlined in greater detail in Chapter 7, "*Financing Structure*".

### ***Employment***

Anglian Water currently employs approximately 3,300 employees. Where Anglian Water employees provide services to the rest of the AWG Group (e.g. payroll), such services are charged out on an arm's length basis.

The costs of any benefits (such as medical expenses insurance) purchased by AWG Group companies (other than Anglian Water) and provided to employees of Anglian Water and other AWG Group companies are similarly shared on an arm's length, pro rata basis. See Chapter 5, "*Ring-fencing and the Anglian Water Services Financing Group*".

### ***Pensions***

The majority of employees in Anglian Water participate in a defined benefit pension scheme (the AWG Pension Scheme ("**AWPS**")). All new employees including senior executives join the AWGDC – defined contribution scheme. A review of future pension arrangements within AWPS is currently under way within the AWG Group. The employee representatives of Anglian Water's Company Collective are being consulted as part of the review process. Any changes will be implemented from April 2006 and will only affect future service. For additional information regarding Anglian Water's pension commitments and the effects it would have on, inter alia, Anglian Water's net assets and profit and loss reserve, see Anglian Water's 2005 Annual Report – Notes to the Financial Statements – Note 25 and Section 5.1.8, "*Ring-Fencing and the Anglian Water Services Financing Group – Ring-Fencing – Ongoing Trading Relationship with other AWG Group Companies – Pension Scheme*".

### ***Litigation***

Anglian Water is not currently involved in any proceedings in any court or tribunal likely to have a significant effect on its business.

## CHAPTER 5

### RING-FENCING AND THE ANGLIAN WATER SERVICES FINANCING GROUP

#### 5.1 Ring-fencing

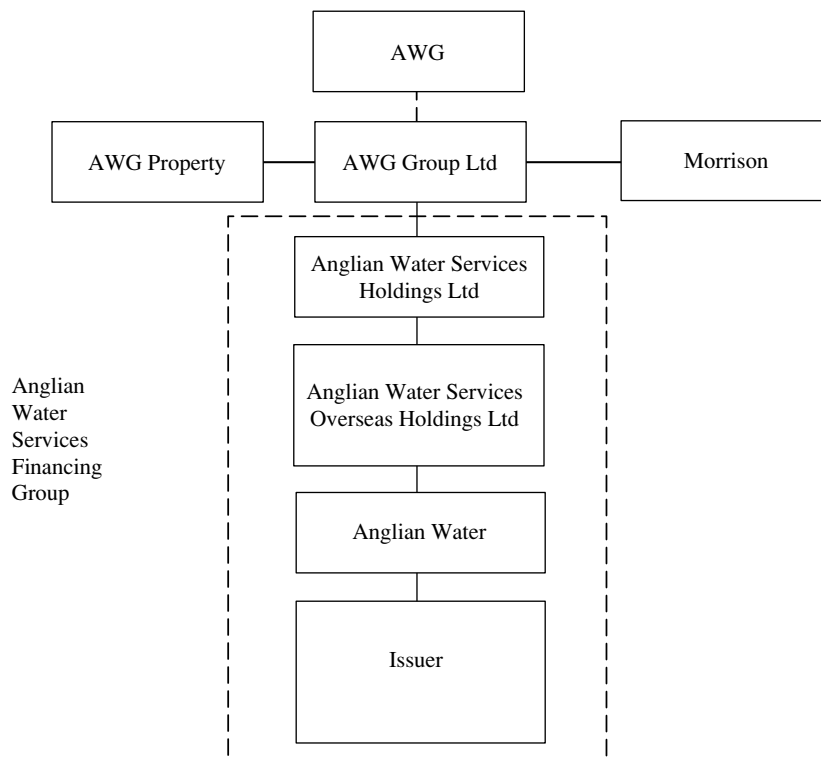
##### 5.1.1 Introduction

As part of its obligations as a Regulated Company, Anglian Water is subject to certain ring-fencing restrictions under its current Licence. See 5.1.2, “*Regulatory Ring-fencing*”. In addition, in July 2002, Ofwat modifications to Anglian Water’s Licence further strengthened the regulatory ring-fencing. See Chapter 12, “*Modifications made to Anglian Water’s Licence*”.

In addition, to reduce Anglian Water’s exposure to credit and event risk of other AWG Group companies, the AWG Group created a new “ring-fenced” financing group (being the “**Anglian Water Services Financing Group**”). These measures also reflect the requirements of the covenant and security package as summarised in Chapter 7, “*Financing Structure*”.

The ring-fencing measures are intended to ensure: (i) that Anglian Water has the means to conduct its regulated business separately from the AWG Group; and (ii) that all dealings between the AWG Group and the Anglian Water Services Financing Group are on an arm’s length basis.

The ownership structure of the Anglian Water Services Financing Group is as follows:



The main elements comprising the structural and legal ring-fencing of the Anglian Water Services Financing Group from the other AWG Group companies are set out below.

##### 5.1.2 Regulatory Ring-fencing

Regulatory ring-fencing is common in differing degrees to each of the Regulated Companies in England and Wales pursuant to their respective licences. Under Condition F of its Licence, as supplemented by RAG 5, Anglian Water must ensure that transactions between it and its associated companies in the AWG Group are on an arm’s length basis, to prevent cross subsidisation of activities. Failure to comply with RAG 5 may in certain circumstances give rise to a breach of the Licence and possibly the Competition Act 1998. See Chapter 11, “*Regulation of the Water and Sewerage Industry in England and Wales*”. Under Condition K of its Licence, Anglian Water must ensure at all times, so far as reasonably practicable, that if a Special

Administration Order was made in respect of it, Anglian Water would have available to it sufficient rights and assets (other than financial resources) to enable the Special Administrator to manage its affairs, business and property so that the purposes of such order could be achieved. See Section 11.5, “*Regulation of the Water and Sewerage Industry in England and Wales – Special Administration Orders*”.

In July 2002, Ofwat modifications to Anglian Water’s Licence strengthened the ring-fencing provisions of the Licence. See Chapter 12, “*Modifications made to Anglian Water’s Licence*”.

### **5.1.3 Corporate Structure**

The regulatory ring-fencing measures described above have been enhanced by the separation of Anglian Water from the other businesses of the AWG Group through the interposition of two intermediate special purpose holding companies, Anglian Water Services Holdings Ltd, incorporated in England and Wales and Anglian Water Services Overseas Holdings Ltd, incorporated in the Cayman Islands. Anglian Water Services Holdings Ltd is a wholly-owned subsidiary of AWG Group Ltd. The principal purpose of Anglian Water Services Holdings Ltd is to hold all of the shares in Anglian Water Services Overseas Holdings Ltd and the principal purpose of Anglian Water Services Overseas Holdings Ltd is to hold all of the shares in Anglian Water.

### **5.1.4 Directors**

Pursuant to the Licence, each company in the Anglian Water Services Financing Group maintains at least three independent non-executive directors. The board of directors of each company in the Anglian Water Services Financing Group may comprise directors who are also directors of other AWG Group companies outside the Anglian Water Services Financing Group so long as any executive directors in this category do not constitute a majority of the executive directors of such company. Currently, Jonson Cox (Group Chief Executive of AWG) is Chairman and Chief Executive of Anglian Water, Scott Longhurst (Group Finance Director of AWG) is a non-executive director of Anglian Water and David Hipple (a director of AWG Holdings Ltd) is the Finance Director of Anglian Water. The Board also currently comprises the other executive directors Peter Simpson, Chris Newsome and Jean Spencer, none of whom are directors of any AWG Group companies outside the Anglian Water Services Financing Group.

The constitutional documents of each company in the Anglian Water Services Financing Group provide that all conflicts of interest of directors must be disclosed. No director may vote on any contract, transaction or arrangement between a company in the Anglian Water Services Financing Group and any other company in the AWG Group, other than a company in the Anglian Water Services Financing Group of which he is a director. All directors are entitled to vote on the matter of dividends and distributions to AWG Group companies.

The Common Terms Agreement provides that following the occurrence of a Trigger Event and if the Trigger Event has not otherwise been remedied or waived, the Security Trustee is entitled to procure the appointment of additional non-executive directors to the board of Anglian Water and a similar entitlement applies in relation to the other companies in the Anglian Water Services Financing Group (the “Security Trustee Directors”). See Section 7.5.8, “*Trigger Event Consequences*”. The articles of association of each company in the Anglian Water Services Financing Group provide that the total number of votes capable of being cast by Security Trustee Directors in respect of any question arising at a meeting of the Directors cannot exceed the total number capable of being cast by the other Directors participating in the meeting in respect of that question. Additionally, the articles of association of each company in the Anglian Water Services Financing Group provide that no Security Trustee Director may be appointed chairman or vote on any resolutions concerning the appointment or removal of a chairman.

There are no potential conflicts of interests between any duties to the Issuer of its Directors and their private interests or duties.

### **5.1.5 Management Compensation**

Following the implementation of the ring-fencing, the Board of Anglian Water has implemented a remuneration policy for executive directors and senior management which creates incentives to

deliver benefits for Anglian Water's lenders (including Bondholders and holders of finance leases), Anglian Water's shareholder and customers. The policy includes the following:

- (a) an annual bonus scheme which measures Anglian Water, team and individual performance against financial and non-financial targets including:
  - maximising sustainable returns, satisfying lenders' requirements and outperforming the five-year price determination set by Ofwat; and
  - improvements in health and safety and service performance; and
- (b) a longer-term scheme which compares the performance of AWG primarily against a peer group of mainly UK water and waste-water companies. AWG shares are considered to be a proxy for Anglian Water shares.

Under management's remuneration policy, executive directors and senior management are incentivised on the basis of Anglian Water's financial and operating performance and are eligible for bonuses of a percentage of base salary.

### **5.1.6 Security and Covenant Packages**

In connection with the restructuring of Anglian Water, the Anglian Water Services Financing Group provided as full a security package as was commensurate with the limitations imposed by the WIA and the Licence.

Pursuant to the covenant package (as set out in Section 7.5.3, "*Financing Structure – Common Terms Agreement – Covenants*"), dividends, management fees (if any), repayments under the UK Holdco/Anglian Water Loan, Customer Rebates and other such distributions are only permitted provided that no Trigger Event or Event of Default is continuing and historical and forward-looking interest cover ratios and regulated asset ratios and certain other conditions are met. In addition, the companies in the Anglian Water Services Financing Group may incur new financial indebtedness to make Restricted Payments only if certain additional ratio tests are met. The security package and the covenant-based ring-fencing restrictions placed on the Anglian Water Services Financing Group are set out in Chapter 7, "*Financing Structure*".

### **5.1.7 Business Separation**

Following the corporate restructuring, Anglian Water operates as a separate corporate entity from the other AWG Group businesses. The AWG Group achieved this separation to the fullest extent practicable by asset and business transfers and by ensuring that contracts between Anglian Water and AWG Group companies were entered into on an arm's length basis. In addition, all existing and new debt as at the Initial Issue Date relating to the regulated water and sewerage business was transferred to and issued by the Issuer, or in certain limited circumstances, Anglian Water, thereby severing any financing links between the Anglian Water Services Financing Group and other companies in the AWG Group.

Pursuant to the ring-fencing, Anglian Water has access to all employees required to run the regulated business. The majority of such employees are employed by Anglian Water.

The general health and safety policy for the AWG Group is set by AWG but Anglian Water-specific policy, procedures and administration are carried out by Anglian Water.

All transactions entered into by the Anglian Water Services Financing Group with third parties (including AWG Group companies) are entered into on an arm's length basis. Any transaction between Anglian Water and the AWG Group is formally reviewed to ensure compliance with the Licence, RAG 5 and procurement regulations. The DGWS included in the Licence additional procurement, procedural and reporting requirements upon Anglian Water. See Chapter 12, "*Modifications made to Anglian Water's Licence*".

As part of the ring-fencing, Anglian Water's activities are restricted to the business of a Regulated Company in England and Wales. Anglian Water's management has retained some non-regulated business and assets within permitted *de minimis* levels (for example, providing certain recreational water activities in or around its reservoirs). Under the covenant package, the Security Trustee may

permit Anglian Water to enter into limited joint ventures in areas outside the regulated water and sewerage business subject to certain limitations on the aggregate value of all non-regulated business. See Chapter 7, “*Financing Structure*”.

Under the covenant package, Anglian Water is able to acquire assets or make disposals only if conditions relating to each are met (for example, regulated asset ratio requirements in relation to disposals). See Section 7.5.5, “*Financing Structure – Common Terms Agreement – Covenants – General*”.

### **5.1.8 Ongoing Trading Relationships with other AWG Group companies**

#### *Pension Scheme*

Anglian Water participates in the same retirement benefit arrangements as other companies in the AWG Group, including in the AWPS. Currently, nearly all Anglian Water employees participate in the AWPS. The ring-fencing programme does not segregate Anglian Water’s pension arrangements from those of the AWG Group, as management believes that it is not cost effective to do so. However, Anglian Water’s contributions to the AWPS are made in respect of Anglian Water’s employees only. Anglian Water has entered into agreements with the other AWG Group companies participating in the AWPS to provide that these companies will withdraw from the AWPS if they are unable to meet their contribution obligations. Transfer payments made out of the AWPS in respect of employees of the withdrawing employer reflect any failure on the part of the withdrawing employer to pay contributions. These measures are intended to minimise the risk of any cross-subsidy within the AWPS between Anglian Water and other AWG Group companies.

In November 2000, the Accounting Standards board issued Financial Reporting Standard 17 (Retirement Benefits) (“**FRS 17**”). As permitted by FRS 17, Anglian Water has adopted its disclosure requirements only. For additional information regarding Anglian Water’s pension commitments and the effects FRS 17 would have on, inter alia, Anglian Water’s net assets and profit and loss reserve, see Anglian Water’s 2005 Annual Report – Notes to the Financial Statements – Note 26.

#### *Intellectual Property (“IP”)*

Other than technology it owns jointly with third parties, Anglian Water does not own any of the intellectual property used in connection with its regulated businesses. However, the Anglian Water water and sewerage businesses do not depend heavily on IP and, apart from software licences, there are no significant “licences-in” of third-party IP. Currently, Anglian Water has organised its IP requirements in conjunction with the AWG Group. As part of an AWG Group IP-pooling arrangement implemented in 1999, Anglian Water and other AWG Group companies assigned their current and future IP (including trade marks, patents and copyright) to AW Creative Technologies Limited (“**AWCT**”), a wholly-owned subsidiary of AWG. Anglian Water has established sufficient licensing arrangements with AWCT’s licensing subsidiary, AW Licensing Limited, to ensure that Anglian Water will continue to have access to all the IP rights it requires to operate its business. Anglian Water’s management does not believe that there are any significant RAG 5 compliance issues in respect of Anglian Water’s IP arrangements. The IP-pooling arrangements are currently under review.

## **5.2 The Anglian Water Services Financing Group**

### **5.2.1 Anglian Water Incorporation, Board of Directors and Corporate Governance**

#### *Company Details*

Anglian Water is a private limited company which was incorporated in England and Wales on 1 April 1989 under the Companies Act with registered number 2366656. The registered office and headquarters of Anglian Water are at Anglian House, Ambury Road, Huntingdon, Cambridgeshire PE29 3NZ.

Anglian Water’s authorised and issued share capital is £860,000,000 divided into 860,000,000 ordinary shares of £1 each. All ordinary shares have been issued and have been fully paid-up.

The business address of the directors of Anglian Water is Anglian House, Ambury Road, Huntingdon, Cambridgeshire, PE29 3NZ and the telephone number is 01480 323 000.

The auditors of Anglian Water are PricewaterhouseCoopers LLP, chartered accountants. The joint company secretaries of Anglian Water are Patrick Firth and Claire Russell.

### ***Directors of Anglian Water***

Anglian Water operates under the overall direction of Anglian Water's Board of Directors (the "**Board**") which is responsible for policy and strategic matters. The Board currently consists of an Executive chairman, four executive directors and four non-executive directors of whom three are independent. All of the directors of Anglian Water are also directors of the Issuer, Anglian Water Services Holdings Ltd and Anglian Water Services Overseas Holdings Ltd.

### ***Executive Chairman***

#### **Jonson Cox**

Jonson Cox was appointed Chief Executive of AWG and Deputy Chairman of Anglian Water in January 2004. In November 2004 he became Executive Chairman of Anglian Water. He was a director of Kelda Group Plc from 1994 to 2000 where he led the recovery of Yorkshire Water, Kelda's principal business. Immediately before joining AWG he was Chief Executive of business services provider Valpak Limited from 2002 to the end of 2003 and Chief Operating Officer of Railtrack Plc from 2000 to 2001.

### ***Executive Directors***

#### **Peter Simpson – Chief Operating Officer**

Peter Simpson was appointed Chief Operating Office in November 2004. He previously held positions within the international division of AWG including Regional Director for Europe based in the Czech Republic and Senior Vice President of Operations based in the USA. Peter is a Chartered Water and Environmental Manager and holds an MBA from Warwick Business School.

#### **David Hipple**

David Hipple was appointed in November 2001. He previously held the offices of Accounting Manager, Finance and Performance Manager and Head of Performance of Anglian Water. He became a Member of the Institute of Chartered Accountants in 1981.

#### **Jean Spencer**

Jean Spencer was appointed in May 2004. She previously held the office of Head of Regulation at Yorkshire Water. She is a chartered accountant.

#### **Chris Newsome**

Christopher Newsome was appointed in September 2004. He joined Anglian Water from Yorkshire Water where he held the offices of Network Technology Manager from 1990 to 1991, Water Systems Manager from 1991 to 1993, General Investment Manager from 1996 to 2000 and most recently Head of Investment. He is a chartered civil engineer, a member of the Institute of Civil Engineers and holds an MBA from Manchester Business School.

#### **Scott Longhurst**

Scott Longhurst was appointed Group Finance Director of AWG in November 2004. Prior to joining AWG, he held a number of positions with TXU Corporation between 2000 and November 2004, including Chief Financial Officer and Senior Vice President, Oncor Group, USA and Group Financial Controller and Chief Accounting Officer, TXU Corporation. Between 1991 and 2000 he held a number of UK and international financial and commercial roles with Royal Dutch/Shell Group including Chief Financial Officer of oil products joint ventures in Saudi Arabia between 1997 and 2000. He is a Fellow of the Institute of Chartered Accountants in England and Wales.

#### **Robert Napier – Independent Non-Executive Director**

Robert Napier was appointed in February 2002. He held the offices of Finance Director of Fison Plc's global pharmaceuticals division and Finance Director, Joint Managing Director, Managing Director and Chief Executive of Redland Plc. He is currently Chief Executive of WWF-UK and Chairman of Governors for Sedbergh School. He was recently appointed a Non-Executive Director of English Partnerships.



### **John Watkinson – Independent Non-Executive Director**

John Watkinson was appointed in May 2005. He has over twenty years experience in a variety of roles, encompassing buying, supply chain and operations, for high profile, brand-led retail businesses. For most of the nineties, John held successive Operations Director roles for both Habitat and Wallis. In 1999, he joined Hamleys plc as its Chief Operating Officer and oversaw the creation and expansion of the highly successful Bear Factory retail concept which now operates in twelve countries across the world. In 2003, John led a successful management buyout of the company and became the Chief Executive of the newly-formed Hamleys Group, a position he held until September this year. John and his family live close to Huntingdon and have been customers of Anglian Water for over twelve years.

### **Roger Witcomb – Independent Non-Executive Director**

Roger Witcomb was appointed in March 2002. He previously held the positions of Group Finance Director and Director of Strategy and Planning of National Power Plc. He is currently a Senior Adviser at Actis Capital LLP. He is a director of Globeleq Ltd and Chairman of the Trustees of Opportunity International UK.

### ***Corporate Governance***

Under its memorandum of association, Anglian Water's primary objects are to carry on the business of a water and sewerage undertaker and to act as a holding company of the Issuer.

Anglian Water's independence from its ultimate holding company, AWG, is enhanced by the inclusion of the following provisions in Anglian Water's articles of association:

- the composition of the board of directors of Anglian Water will include a minimum number of three non-executive directors who are not directors of any company in the AWG Group (outside of the Anglian Water Services Financing Group) and who are not employees of any company in the AWG Group;
- the board of directors of Anglian Water will not have a majority of executive directors who serve on any other boards within the AWG Group, outside of the Anglian Water Services Financing Group; and
- any Anglian Water director who serves on any boards of directors within the AWG Group will be disqualified from voting in respect of any contracts, transactions and arrangements between Anglian Water and any other company in the AWG Group (or any subsidiary of it) in which he is interested by virtue of being a director of that other company (save for any contracts, transactions and arrangements between Anglian Water and the companies in the Anglian Water Services Financing Group).

Equivalent provisions are included in the articles of association of the Issuer, Anglian Water Services Holdings Ltd and Anglian Water Services Overseas Holdings Ltd. Subject to the above provisions relating to the composition of the Anglian Water Board, AWG, as ultimate holding company, may appoint the directors of the Board of Anglian Water and of the other companies in the Anglian Water Services Financing Group. All directors are entitled to vote on the matter of dividends and distributions to AWG Group companies.

The directors of Anglian Water support high standards of corporate governance and have due regard to the Combined Code (the Principles of Good Governance and Code of Best Practice appended to the Listing Rules of the Financial Services Authority). To this end, in early 2002, Anglian Water established an Audit Committee. Anglian Water has established management systems to ensure compliance with health and safety and environmental regulations in respect of water quality and sewage disposal. Anglian Water is also subject to the provisions of the Companies Act.

Anglian Water is pursuing a sustainable development strategy and has put in place corporate governance structures to ensure this strategy is implemented and reviewed. A sustainable development report is produced each year which is subject to independent assessment and also to comment by stakeholders including campaign groups and financial institutions.

### **Directors' Interests**

The interests of the directors of Anglian Water in AWG's share capital are as follows:

<i>Director</i>	<i>Number of Ordinary Shares (including beneficial and family interest) as at 26 July 2005</i>	<i>Interests in Contingent Shares as at 26 July 2005<sup>(1)</sup></i>	<i>Interests in Options as at 26 July 2005<sup>(2)</sup></i>
Jonson Cox .....	16,396	180,218	230,363
Scott Longhurst .....	1,184	56,744	—
Peter Simpson .....	4,686	39,088	48,714
David Hipple .....	1,348	23,386	12,542
Chris Newsome .....	610	19,239	1,276
Jean Spencer .....	930	20,973	2,227
Robert Napier .....	—	—	—
Roger Witcomb .....	—	—	—
John Watkinson .....	—	—	—

Notes:

- (1) All directors have received awards of Matching Shares under the AWG Plc Annual Retained Bonus Scheme and the AWG Plc Long Term Incentive Plan. The extent of vesting for both awards is contingent on the achievement of certain performance targets.
- (2) Jonson Cox's interests include options granted under the AWG Plc Sharesave Scheme, the AWG Plc Executive Share Option Scheme and a Phantom Award granted under the schedule to that scheme. Peter Simpson's and David Hipple's interests comprise grants made under the AWG Plc Executive Share Option Scheme and the AWG Plc Sharesave Scheme. Chris Newsome's and Jean Spencer's interests comprise grants made under the AWG Plc Sharesave Scheme.

### **Subsidiaries**

At the date of this Prospectus Anglian Water has no subsidiaries other than the Issuer.

#### **5.2.2 The Issuer**

The Issuer was incorporated and registered in England and Wales under the Companies Act with limited liability as Precis (2157) Limited, a private limited company, on 28 November 2001 with registered number 4330322. On 10 January 2002, it changed its name to Anglian Water Services Financing Limited. It was re-registered as a public limited company on 7 March 2002. The registered office of the Issuer is at Anglian House, Ambury Road, Huntingdon, Cambridgeshire PE29 3NZ and its telephone number is 01480 323 000.

The Issuer is a wholly-owned direct subsidiary of Anglian Water and an indirect subsidiary of AWG. Its authorised share capital is £100,000 divided into 100,000 ordinary shares of £1 each and it has an issued share capital of £12,502. 50,000 ordinary shares have been issued, of which 49,998 have been issued quarter paid-up and two are fully paid-up. The Issuer has no subsidiaries.

#### **Directors and Joint Company Secretaries of the Issuer**

The directors of the Issuer are Jonson Cox, Peter Simpson, David Hipple, Chris Newsome, Jean Spencer, Scott Longhurst, Robert Napier, John Watkinson and Roger Witcomb and their principal activities are described in 5.2.1, "*Anglian Water Incorporation, Board of Directors and Corporate Governance*".

The business address of the directors of the Issuer is Anglian House, Ambury Road, Huntingdon, Cambridgeshire PE29 3NZ.

The joint company secretaries of the Issuer are Patrick Firth and Claire Russell.

#### **The Activities of the Issuer**

The Issuer has no employees nor does it own any physical assets. Administration and treasury functions are conducted on its behalf by Anglian Water. It is intended to conduct all future

financing activities (save for financing lease arrangements) for the Anglian Water Services Financing Group through the Issuer. The Issuer has issued various series of Bonds. The Issuer has entered into: (i) the Debt Service Reserve Liquidity Facility Agreements to enable it to borrow monies in order to fund liquidity shortfalls in respect of Bonds and other financial indebtedness of the Issuer and the Authorised Loan Agreement; (ii) Hedging Agreements in accordance with the Hedging Policy; (iii) the O&M Reserve Facility Agreement; and (iv) any other documents incidental to the Programme. See Chapter 7, “*Financing Structure*”.

The Issuer is empowered under its memorandum and articles of association to enter into the proposed transaction documents to which it is a party and its directors have authority under the Issuer’s articles of association to exercise that power on its behalf.

The Issuer’s auditors are PricewaterhouseCoopers LLP, chartered accountants.

### **5.2.3 Anglian Water Services Overseas Holdings Ltd**

Anglian Water Services Overseas Holdings Ltd was incorporated in the Cayman Islands on 16 January 2002 as an exempted company with limited liability, with registered number 115224.

Anglian Water Services Overseas Holdings Ltd is a wholly-owned subsidiary of Anglian Water Services Holdings Ltd and an indirect subsidiary of AWG. Its authorised share capital is £300,000,000 divided into 300,000,000 ordinary shares of £1 each. All shares have been issued and are fully paid up. Anglian Water Services Overseas Holdings Ltd has no other equity or debt capital.

Anglian Water Services Overseas Holdings Ltd has its registered office at P.O. Box 309, Uglan House, South Church Street, George Town, Grand Cayman, Cayman Islands and its telephone number is +1 345 949 8066.

#### ***Directors and Joint Company Secretaries of Anglian Water Services Overseas Holdings Ltd***

The directors of Anglian Water Services Overseas Holdings Ltd are Jonson Cox, Peter Simpson, David Hipple, Chris Newsome, Jean Spencer, Scott Longhurst, Robert Napier, John Watkinson and Roger Witcomb and their principal activities are described in 5.2.1, “*Anglian Water Incorporation, Board of Directors and Corporate Governance*”.

The business address of the directors of Anglian Water Services Overseas Holdings Ltd is Anglian House, Ambury Road, Huntingdon, Cambridgeshire PE29 3NZ.

The joint company secretaries of Anglian Water Services Overseas Holdings Ltd are Patrick Firth and Claire Russell.

#### ***The Activities of Anglian Water Services Overseas Holdings Ltd***

Anglian Water Services Overseas Holdings Ltd is managed in such a way as to ensure that it is resident for tax purposes in the United Kingdom. Anglian Water Services Overseas Holdings Ltd has no employees nor does it own any physical assets other than its shares in Anglian Water. Administration and treasury functions are conducted on its behalf by Anglian Water and certain third parties, including the Cayman Islands law firm Maples and Calder.

The principal activity of Anglian Water Services Overseas Holdings Ltd is to hold the shares of Anglian Water and to enter into documents incidental to the Programme. Anglian Water Services Overseas Holdings Ltd has no direct subsidiaries other than Anglian Water. Anglian Water Services Overseas Holdings Ltd is empowered under its memorandum and articles of association to enter into the proposed transaction documents to which it is party and its Directors have authority under Anglian Water Services Overseas Holdings Ltd’s articles of association to exercise that power on its behalf.

The activities of Anglian Water Services Overseas Holdings Ltd are restricted in the Common Terms Agreement. See Section 7.5.5, “*Financing Structure – Common Terms Agreement – Covenants – General*”.

Anglian Water Services Overseas Holdings Ltd, being an exempted company incorporated with limited liability under the laws of the Cayman Islands, is not obliged by statute but nevertheless

has decided to prepare audited accounts. The auditors of Anglian Water Services Overseas Holdings Ltd are PricewaterhouseCoopers LLP, chartered accountants.

#### **5.2.4 Anglian Water Services Holdings Ltd**

Anglian Water Services Holdings Ltd was incorporated in England and Wales under the Companies Act as a limited liability company on 28 November 2001 under the name of Precis (2158) Limited, with registered number 4330144. Anglian Water Services Holdings Ltd changed its name to Anglian Water Services Holdings Limited on 10 January 2002. The registered office of Anglian Water Services Holdings Ltd is at Anglian House, Ambury Road, Huntingdon, Cambridgeshire PE29 3NZ and its telephone number is 01480 323 000.

Anglian Water Services Holdings Ltd is a wholly-owned direct subsidiary of AWG Group Ltd and an indirect subsidiary of AWG. Its authorised share capital is £100 divided into 100 ordinary shares of £1 each. Two ordinary shares have been issued to AWG Group Ltd and are fully paid-up.

##### ***Directors and Joint Company Secretaries of Anglian Water Services Holdings Ltd***

The directors of Anglian Water Services Holdings Ltd are Jonson Cox, Peter Simpson, David Hipple, Chris Newsome, Jean Spencer, Scott Longhurst, Robert Napier, John Watkinson and Roger Witcomb and their principal activities are described in 5.2.1 “*Anglian Water Incorporation, Board of Directors and Corporate Governance*”.

The business address of the directors of Anglian Water Services Holdings Ltd is Anglian House, Ambury Road, Huntingdon, Cambridgeshire PE29 3NZ.

The joint company secretaries of Anglian Water Services Holdings Ltd are Patrick Firth and Claire Russell.

##### ***The Activities of Anglian Water Services Holdings Ltd***

Anglian Water Services Holdings Ltd has no employees nor does it own any physical assets other than its shares in Anglian Water Services Overseas Holdings Ltd. Administration and treasury functions are conducted on its behalf by Anglian Water.

The principal activity of Anglian Water Services Holdings Ltd is to hold the shares of Anglian Water Services Overseas Holdings Ltd and to enter into documents incidental to the Programme. Anglian Water Services Holdings Ltd has no direct subsidiaries other than Anglian Water Services Overseas Holdings Ltd.

Anglian Water Services Holdings Ltd is empowered under its memorandum and articles of association to enter into the proposed transaction documents to which it is a party and its Directors have authority under Anglian Water Services Holdings Ltd’s articles of association to exercise that power on its behalf.

The activities of Anglian Water Services Holdings Ltd are restricted in the Common Terms Agreement. See Section 7.5.5, “*Financing Structure – Common Terms Agreement – Covenants – General*”.

Anglian Water Services Holdings Ltd’s auditors are PricewaterhouseCoopers LLP, chartered accountants.

## CHAPTER 6

### RISK FACTORS

The following is a summary of certain aspects of the issue of the Bonds and related transactions about which prospective Bondholders should be aware. The occurrence of one or more of the events discussed below could have a material adverse impact on the business, financial condition or results of operations of the Issuer or the other Obligor or their ability to meet their obligations (including the payment of principal and interest) under the Bonds.

This summary is not intended to be exhaustive and prospective Bondholders should read the detailed information set out elsewhere in this document prior to making any investment decision. Further, any prospective Bondholder should take their own legal, financial, accounting, tax and other relevant advice as to the structure and viability of their investment. Bondholders may lose the value of their entire investment in certain circumstances.

#### 6.1 Regulatory and Competition Considerations

The water industry is subject to extensive legal and regulatory controls, and Anglian Water must comply with all applicable laws, regulations and regulatory standards. The application of these laws, regulations and regulatory standards and the policies of the DGWS or its impending replacement, the WSRA, could have a material adverse impact on the operations and financial condition of Anglian Water.

In this context, in particular, potential investors should be aware of the following:

##### 6.1.1 Licence

Under the WIA, the conditions of Anglian Water's Licence may be modified by the DGWS with or, following a reference to the Competition Commission which concludes that there are effects adverse to the public interest which can be remedied or prevented by modifications, without the consent of Anglian Water. See Section 11.3.3, "*Regulation of the Water and Sewerage Industry in England and Wales – Modification of a Licence*". In addition, the Secretary of State has a power to veto certain proposed modifications agreed by the DGWS and Anglian Water and other proposed modifications which have been agreed by the DGWS and Anglian Water may be vetoed if it appears to the Secretary of State that the modifications should be made, if at all, after a reference to the Competition Commission (hence causing the DGWS to refer the modifications to the Competition Commission). Under the Water Act, the DGWS's powers will be transferred to the WSRA once the latter is created (which is expected in 2006); the Secretary of State's power to veto will remain.

The area of appointment of Anglian Water can also be varied in accordance with a so-called "inset" appointment and under the Water Act a new entrant in Anglian Water's area will be able to obtain a licence to supply non-domestic customers with a consumption of over 50 megalitres a year. See Section 11.10.2 "*Regulation of the Water and Sewerage Industry in England and Wales – The Water Act*". Modifications to the Licence may also be made without Anglian Water's consent by the Secretary of State by order following an adverse finding by the Competition Commission after it has investigated and reported on a monopoly or merger situation under other enactments. Any restrictive modification to the Licence could have a material adverse impact on Anglian Water.

Anglian Water's Licence was modified as part of the restructuring which included modifications concerning procurement of services, control of operations, strengthening of the financial ring-fence, maintenance of an investment grade corporate credit rating, corporate governance and the availability of market and other information. Anglian Water agreed to consent to such modifications subject to changes agreed with Ofwat and on the basis of representations from Ofwat as to how certain of such new or modified Licence conditions will be interpreted and applied by Ofwat. If the Licence conditions are not interpreted and applied in that way this could have a material adverse impact on Anglian Water. See Section 12.2, "*Modifications Made to Anglian Water's Licence – Licence Modifications*".

A failure by Anglian Water to comply with the conditions of its Licence, as modified from time to time may lead to the making of an enforcement order by the DGWS or the Secretary of State,

which could have an adverse impact on Anglian Water. Failure by it to comply with an enforcement order (as well as certain other defaults) may lead to the making of a Special Administration Order (as described below). See Section 11.5, “*Regulation of the Water and Sewerage Industry in England and Wales – Special Administration Orders*”.

Under the terms of the Licence, the Secretary of State may terminate Anglian Water’s appointment without its consent where the Secretary of State has given Anglian Water at least 25 years’ notice and that period of notice has expired. Upon expiry of the Licence, there can be no assurance that Anglian Water would be re-appointed. Anglian Water’s Licence may also be transferred from Anglian Water at any time following the making of a Special Administration Order. The termination, non-renewal or transfer of the Licence could have a material adverse impact on Anglian Water, including on its ability to meet its obligations (including the payment of principal and interest) under the Bonds.

### **6.1.2 Water Act and Competition in the Water Industry**

The Water Act received Royal Assent on 20 November 2003. It contains certain changes to the regulatory system applicable to the water industry. One of the most significant changes in the Water Act is a new power for the DGWS and the Secretary of State to fine a Regulated Company up to 10 per cent. of its turnover if it breaches its licence or fails to meet standards of performance or certain other obligations. The DGWS and the Secretary of State are now required to protect customers’ interests by promoting effective competition in relation to water and sewerage services whenever appropriate as a primary rather than a secondary duty. Also, the Water Act introduces licences for new entrants which will allow them to supply large eligible non-household customers (taking more than 50 megalitres of water per annum) either by taking a wholesale supply of water from a water undertaker or through common carriage and then providing a retail supply to the customer. Common carriage is also put on a statutory basis in order to encourage competition for water services. New entrants can apply for a water supply licence from 1st August 2005 with a view to it taking effect in December 2005. See Section 11.10.2, “*Regulation of the Water and Sewerage Industry in England and Wales – The Water Act*” for further details of these changes. In addition, the Water Act provides that abstraction licences may in certain circumstances be revoked or modified in the interests of environmental protection, including the revocation or variation without compensation of abstraction licences that have not been used for four years. Each of the above changes gives rise to a potential material adverse impact on Anglian Water.

The Competition Act contains prohibitions relating to anti-competitive agreements and conduct and powers of investigation and enforcement. See Section 11.10, “*Regulation of the Water and Sewerage Industry in England and Wales – Competition in the Water Industry*”. These powers include powers for the DGWS to enforce directions bringing an infringement to an end and to impose fines of up to 10 per cent. of worldwide group-wide turnover for the infringement up to a maximum of three years. Also, any agreement which infringes the Competition Act may be void and unenforceable and may give rise to claims for damages from third parties. The Enterprise Act 2002 (the “**Enterprise Act**”) adds further remedies for breach of competition law. The Enterprise Act contains criminal sanctions, including the possibility of imprisonment of individuals who have been involved in certain cartels and directors involved in breach of competition law may be disqualified. Consumer groups are now able to bring actions on behalf of customers (including for damages).

Each Regulated Company under its licence effectively holds a geographical monopoly in its appointed area for the provision of water and sewerage services. However, there is certain limited competition for the provision of water and sewerage services and the Water Act’s provisions for licensing new entrants are intended to increase the scope for competition. Furthermore, the DGWS has stated that he will use his powers under the Competition Act to investigate and prohibit anti-competitive practices, agreements and abuses of a dominant position, to ensure a level playing field in the industry.

Current and proposed methods for introducing or extending competition are outlined in Section 11.10, “*Regulation of the Water and Sewerage Industry in England and Wales – Competition in the Water Industry*”. It is not possible to assess if, or how, such methods will affect the interests of Bondholders. Either the extension of competition within the water industry or the bringing of

proceedings against Anglian Water in respect of its competitive position in the area in which it operates could have a material adverse impact on Anglian Water.

## 6.2 Anglian Water Revenue Considerations

Although: (i) the DGWS has a duty to exercise his powers in the manner that he considers is best calculated, *inter alia*, to ensure that Anglian Water is able to finance the proper carrying out of its functions; and (ii) certain changes in circumstances can trigger adjustments to price limits between Periodic Reviews under the Interim Determination provisions of the Licence, as with any Regulated Company, no assurance can be given that the revenues generated by Anglian Water from its water and sewerage business will be sufficient to enable it to make full and timely payment of amounts due, in respect of the Bonds. See Chapter 4, “*Anglian Water Business Description – Customer Charges*”. In addition to the regulatory and competition risks described above which could adversely affect the revenues of Anglian Water, other potential events which could have a material adverse impact on Anglian Water or result in it having insufficient revenues to meet its financing obligations include:

### 6.2.1 Price Review

Periodic reviews (“**Periodic Reviews**”) of price limits are, at present, carried out at five-yearly intervals by the DGWS, a role that will pass to the WSRA on its creation in 2006. The most recent review was completed in December 2004. There is no assurance that current and/or future price limits will permit the generation of sufficient revenues to enable Anglian Water to carry out its functions. Although the methodology introduced in the 1994 review – in particular the derivation of the “regulatory asset value” as the measure of capital to be remunerated – was also applied with modifications in 1999 and 2004, the DGWS is not required to apply the same or a similar methodology in future reviews. To arrive at his conclusions, the DGWS makes estimates of the scope for operating and capital cost efficiencies using a wide range of comparative techniques. Judgements are also applied in estimating the sector cost of capital in determining whether or not to make allowance for the “embedded” costs of fixed rate debt and in assessing whether additional allowances are required to enable companies to finance their functions.

In carrying out a review, the DGWS sets targets on the basis of his assessment of what constitutes an efficiently managed Regulated Company. On that basis, prices are set so that Regulated Companies revenues cover the cost of the “efficient” provision of operations and capital investment (as determined by the DGWS) including a company specific tax charge, and to allow a reasonable return on capital. However, the DGWS is under no duty to ensure the continued solvency of a Regulated Company in all circumstances and there is no assurance that price limits imposed by the DGWS at such reviews will permit Anglian Water to generate sufficient revenues to enable it to finance its functions or discharge its obligations under the Issuer/Anglian Water Loan Agreement.

If a Regulated Company disputes the DGWS’s price determination, it may require the DGWS to refer the matter to the Competition Commission for determination by it (after making necessary investigations).

As described in Section 11.8.5, “*Regulation of the Water and Sewerage Industry in England and Wales – Interim Determinations of K*”, Interim Determinations of price limits may be made between five-yearly reviews in specified circumstances. In contrast to Periodic Reviews, the methodology to be applied for Interim Determinations is set out in detail in Anglian Water’s Licence and the scope for discretion is narrower. Also, if a Regulated Company disputes the DGWS’s Interim Determination, it can require the DGWS to refer the determination to the Competition Commission. There can, however, be no assurance that if an adjustment is made it will provide adequate revenue compensation to Anglian Water. Either type of determination could have a material adverse impact on Anglian Water.

### 6.2.2 Deviation from DGWS’s Projections

Under Condition B of the Licence, the Retail Price Index (“**RPI**”) + K price cap limits the annual “weighted average increase” in the standard charges of Anglian Water. This, in turn, is calculated by reference to the “tariff basket formula”, which is constructed so as to provide some compensation in respect of certain risks (for example, high rateable value customers opting for a meter), but not others, including movements in the number of customers or movements in volumes

consumed/discharged by customers. Accordingly, at Periodic Reviews the DGWS factors into his projections assumptions about numbers of customers and volumes consumed/discharged. Until the following Periodic Review, Anglian Water bears the risk that actual numbers of customers and volumes consumed/discharged will fall short of the assumptions reflected in the RPI+K price cap. See Section 11.8.3, “*Regulation of the Water and Sewerage Industry in England and Wales – Price Control*”.

### **6.2.3 Optional Metering**

The WIA provides that as from 1 April 2000 in the case of a residential customer opting to pay for water services on a metered basis, the Regulated Company may not recover the expenses of installing the meter. Any resulting shift from unmetered to metered use may lead to short-term revenue losses to Anglian Water, although any loss may be mitigated by the treatment of unmetered charges in the tariff basket formula used to calculate the annual change in Anglian Water’s standard charges. See Chapter 3, “*Management’s Discussion and Analysis of Financial Condition and Results of Operations – Metering*”. In 1999 and 2004 the DGWS determined that the costs and revenue effects of any excess metering above the levels he assumed for each Regulated Company in his five year price determinations would be eligible for an Interim Determination. See Section 11.8.5, “*Regulation of the Water and Sewerage Industry in England and Wales – Interim Determinations of K*”. The shift from unmetered to metered use could have a material adverse impact on the financial condition or operations of Anglian Water. See Chapter 3, “*Management’s Discussion and Analysis of Financial Condition and Results of Operations – Metering*”.

### **6.2.4 Weather**

Anglian Water is at risk during periods of heavy rainfall. Regulated Companies have a duty to undertake works to minimise the risk of damage from sewage flooding. As part of the regulatory contract for AMP4, the DGWS has made allowance for, and Anglian Water has a commitment to undertake a programme of works substantially to reduce the number of properties at risk of internal and external sewerage flooding. See Section 11.9, “*Regulation of the Water and Sewerage Industry in England and Wales – Drinking Water and Environmental Regulation*” below.

Anglian Water is also at risk from the effects of prolonged periods of drought. If there are supply shortfalls, additional costs may be incurred to provide emergency reinforcement to supplies in areas of shortage. Restrictions on water use may adversely affect revenues from metered customers and may lead to compensation having to be paid to customers who suffer interruptions in supply under Condition Q of the Licence. See Section 11.11.3, “*Regulation of the Water and Sewerage Industry in England and Wales – Guaranteed Standards*”.

## **6.3 Certain Legal Considerations**

### **6.3.1 Security**

Anglian Water’s ability to grant security over its assets and the enforcement of such Security are restricted by its Licence and the WIA. The substantial majority of Anglian Water’s assets by value are tangible property which is either Protected Land, (as defined in the WIA) and/or are assets which are required for the carrying out of Anglian Water’s Regulated Business and cannot therefore be effectively secured (at least, in the case of Protected Land, without the prior consent of the DGWS). The extent of Anglian Water’s ability to grant security over its intangible property (including receivables) is also uncertain. In addition, Anglian Water’s ability to generate receivables is dependent, in any event on its continuing to hold the Licence.

The DGWS has confirmed that the guarantees given under the Security Documents will not be prohibited under the modifications to Condition F6.11(1A) of Anglian Water’s Licence but he has not been asked to consent, and has not consented to, the granting of the Security. The DGWS has requested that Anglian Water and the Issuer make clear to all investors that all security granted by Anglian Water over the assets of the Regulated Business is subject to the WIA and to ensure that all investors understand that this, in effect, means that such security could not be enforced. This reflects the opinion of Ofwat which is not necessarily a definitive statement of the legal position in all respects and circumstances but investors should not over-estimate the value of the security created by Anglian Water nor under-estimate the difficulties that may be incurred if ever they wish to enforce that security.



The Secretary of State and the DGWS have rights under the WIA to appoint a Special Administrator in certain circumstances in respect of Anglian Water and its business. The appointment of a Special Administrator effectively places a moratorium upon any holder of security from enforcing that security. Under the WIA, there is no right to block the appointment of a special administrator equivalent to the right that a holder of a floating charge over the whole or of substantially the whole of the business of a non regulated company may have, in certain circumstances, to block the appointment of a conventional Insolvency Act administrator.

There are also certain legal restrictions which arise under the WIA and the Licence affecting the enforcement of the security created under the Security Agreement executed by Anglian Water. For example, such enforcement is prohibited unless the person enforcing the security has first given 14 days' notice to the DGWS or the Secretary of State hence giving time for him to exercise his rights under the WIA if he is so able and so chooses. See 6.3.2, "*Special Administration*" below. See also Section 11.7, "*Regulation of the Water and Sewerage Industry in England and Wales – Security*".

Accordingly, the security provided over the assets of Anglian Water to the Secured Creditors affords significantly less protection to the Secured Creditors than would be the case if Anglian Water were not a Regulated Company subject to the WIA and its Licence.

The considerations described above do not apply to the fixed and floating charges comprised in the Security Agreement executed by Anglian Water Services Overseas Holdings Ltd, Anglian Water Services Holdings Ltd and the Issuer. The enforcement of security over the shares in any company in the Anglian Water Services Financing Group, (other than the Issuer) including those granted by any holding company of Anglian Water, would not be subject to the moratorium on the enforcement of security rights imposed upon Secured Creditors under the WIA if a Special Administrator is appointed, nor would the enforcement of those share charges be an event which would itself result in the making of a Special Administration Order. However, it is anticipated that any intended enforcement directly or indirectly of the Security Agreement executed by Anglian Water Services Overseas Holdings Ltd and Anglian Water Services Holdings Ltd or the security over, and subsequently any planned disposal of, the shares in Anglian Water (over which a fixed equitable charge is being granted) would require consultation with the DGWS.

In addition, no notice of the security created pursuant to the Security Documents is to be given to customers of Anglian Water prior to the occurrence of an Event of Default. No charge over Anglian Water's land purported to be granted is intended to be (or, indeed in most cases, capable of being) registered with HM Land Registry. Until the Security Trustee enforces its security interests in respect of this charge, the charge will take effect (if at all) in equity only and, thus, will be subject to prior equities and/or certain other legal rights arising in relation thereto. The security interests granted in favour of the Security Trustee over the shares of the Obligors are not to be legally perfected prior to the occurrence of an Event of Default and the Security Trustee may not become the relevant legal owner until such later date. Until they are perfected, these security interests will take effect in equity only and, thus, will be subject to prior equities and/or certain other legal rights arising in relation thereto.

If any Obligor were to go into administration or liquidation within two years of the granting of the security then any floating charge created could be invalid except to the extent of monies paid, or services supplied to it at the same time or after the creation of the Security.

As a result, the amount and nature of the security interest provided in respect of the Bonds may not be sufficient to provide payment of amounts due and owing in respect of the Bonds.

### **6.3.2 Special Administration**

The WIA contains provisions enabling the Secretary of State or the DGWS, with the consent of the Secretary of State, to secure the general continuity of water supply by petitioning the Court for the appointment of a Special Administrator in certain circumstances (for example, including where Anglian Water is unable, or is unlikely to be able, to pay its debts or is in breach of the terms of its Licence). In addition, in certain circumstances, a petition by a creditor of Anglian Water to the Court for the winding-up of Anglian Water might result in the appointment of a Special Administrator. Under the Water Act, the DGWS's powers in this regard will pass to the WSRA,

once it is created in 2006. See Section 11.5, “*Regulation of the Water and Sewerage Industry in England and Wales – Special Administration Orders*”.

During the period of a Special Administration Order, Anglian Water would have to be managed by the Special Administrator for the purposes of the order and in a manner which protects the interests of members, customers and creditors. While the order is in force, no steps may be taken to enforce any security over Anglian Water’s property except with the consent of the Special Administrator or the leave of the Court. Subject to the WIA, the Licence and, in particular Condition K, a Special Administrator would be able to dispose of assets free of any floating charge existing in relation to them.

The purposes of a Special Administration Order consist of: (i) transferring to one or more other companies as much of the business of the Regulated Company in Special Administration as is necessary in order to ensure that the functions which have been vested in such Regulated Company by virtue of its licence are properly carried out; and (ii) pending the transfer, the carrying out of those functions. Accordingly, the Special Administrator may not accept an offer to purchase the assets on a break-up basis in circumstances where the purchaser would be unable properly to carry out the relevant functions of a Regulated Company, even if such offer were at a higher price. See Section 11.5, “*Regulation of the Water and Sewerage Industry in England and Wales – Special Administration Orders*”.

### **6.3.3 Insolvency Act 2000**

The Insolvency Act 2000 (the “**Insolvency Act 2000**”) received Royal Assent on 30 November 2000. The Act amends Part I of the Insolvency Act 1986 so that the directors of a company which meets certain eligibility criteria (an “**eligible company**”) can take steps to obtain a moratorium the effect of which, *inter alia*, would prevent any creditor enforcing security or taking proceedings to recover its debt for the period in which the moratorium is in force. The relevant provisions came into force on 1 January 2003. However, prior to bringing the provisions into force, the Secretary of State amended the eligibility criteria by way of statutory instrument in such a way that utility companies like Anglian Water and special purpose vehicles such as the Issuer, Anglian Water Services Overseas Holdings Ltd and Anglian Water Services Holdings Ltd could no longer be considered to be eligible companies. It is possible that the Secretary of State could in the future modify the present definition of an “eligible company”.

## **6.4 Environmental and Insurance Considerations**

### **6.4.1 Environmental**

Anglian Water’s water supply and sewerage operations are subject to a number of laws and regulations relating to the protection of the environment and human health governed primarily by the DWI and the EA as described in Chapter 11, “*Regulation of the Water and Sewerage Industry in England and Wales*”.

Although Anglian Water believes that it is in material compliance with all such laws and regulations, it is likely that it will in future incur significant costs in complying with upgrading requirements imposed under existing or future laws and regulations. Although the costs of complying with changes in legal requirements are eligible for the purposes of the Interim Determination provisions, there can be no certainty as to how and whether future laws and regulation will impact the business of Anglian Water and/or the interests of the Bondholders. It is possible that a proportion of the costs incurred by Anglian Water in complying with such laws and regulations will not be covered by funding allowed by the regulator and will, therefore, have to be borne directly by Anglian Water.

Given the nature of Anglian Water’s operations there is a risk that drinking water quality and environmental pollution incidents may occur, the possible consequences of which may be criminal prosecution leading to the imposition of fines on Anglian Water and/or civil liability in damages to third parties and/or a requirement to clean up any contamination and/or an operational requirement to upgrade plant and equipment. Such incidents could also give rise to prosecutions against the directors of Anglian Water. The imposition of fines, civil liability, clean-up costs or upgrade costs may materially and adversely affect the financial position of Anglian Water. Any such incidents may also give rise to breaches of any operational environmental consents held by Anglian Water.

For further information in relation to prosecutions brought against Anglian Water, see Section 11.9, “*Regulation of the Water and Sewerage Industry in England and Wales – Drinking Water and Environmental Regulation*”.

There is also a risk that Anglian Water may incur liability to clean up contamination caused by historical activities at its sites, whether or not Anglian Water caused the contamination in question. The costs of cleaning up contamination of land and/or water may be significant. Such contamination may also result in claims by third parties such as neighbouring landowners.

In addition to environmental costs imposed upon Anglian Water by law or regulation, Anglian Water may be subject to additional costs resulting from public concern regarding environmental matters. For example, farms that use sludge from Anglian Water’s sewerage operations are increasingly requiring higher levels of treatment of this sludge in response to demands from the buyers of their crops. This in turn results in higher capital and operating costs for Anglian Water.

#### **6.4.2 Insurance**

Although Anglian Water maintains insurance (including business interruption insurance) to protect against certain risks, the proceeds of such insurance may not in certain circumstances be adequate to cover reduced revenues, increased expenses or other liabilities which may arise. Moreover, there can be no assurance that such insurance coverage will be available in the future at commercially reasonable rates or at all.

### **6.5 Future Financing**

The Issuer will need to raise further debt from time to time in order to finance future capital enhancements to Anglian Water’s asset base, to refinance any other debt (including for liquidity or working capital purposes) the terms of which have become inefficient or which have a scheduled partial or final maturity prior to the final maturity of the Bonds and, on each Interest Payment Date on which principal is required to be repaid, and on the expected Maturity Date of the relevant class of Bonds, to refinance Bonds. Whilst the Programme contemplates the terms and conditions on, and circumstances under, which such additional debt can be raised, there can be no assurance that the Issuer will be able to raise sufficient funds, or funds at a suitable interest rate, or on suitable terms, at the requisite time such that all amounts then due and payable on the Bonds or any other maturing debt will be capable of being so paid when due.

In addition, the DGWS has stated that he will assess the cost of debt at future price reviews on the basis of a hypothetical efficiently-financed company. According to the DGWS, such a company would retain the flexibility to respond to changing market conditions, and hold a balanced portfolio of debt. There is no guarantee, therefore, that allowance would be made for the costs of then existing fixed-rate debt, if current forward-looking rates at the time were lower and if the DGWS took the view that such debt had not been prudently incurred.

### **6.6 High Leverage**

Anglian Water has indebtedness that is substantial in relation to its shareholders equity. As part of this MTN Programme, Anglian Water has, to date, issued Class A and Class B debt to increase Anglian Water’s gross indebtedness to approximately £4.3 billion. The Anglian Water Services Financing Group at March 2005 is leveraged to almost 100 per cent. as a percentage of total debt to RAV. Taking into account retained cash reserves, the net leverage is 80 per cent. of RAV. The ability of Anglian Water to improve its operating performance and financial results will depend upon economic, financial, competitive, regulatory and other factors beyond its control, including fluctuations in interest rates and general economic conditions in the United Kingdom.

The level of debt of Anglian Water has several important effects on its future operations, including the following: (a) Anglian Water has significant cash requirements to service debt; (b) Anglian Water may be restricted in the future from obtaining additional financing, whether for capital expenditure, working capital or other purposes; and (c) Anglian Water is required to comply with certain financial covenants and other restrictions contained in the Bonds and its other indebtedness, further restricting its financial and operational flexibility.

Accordingly, there can be no assurance as to Anglian Water’s ability to meet its financing requirements and no assurance that Anglian Water’s high degree of leverage will not have a material adverse impact on its ability to pay amounts that will be due and owing in respect of the Bonds. Incurrence of additional

indebtedness by Anglian Water, the Issuer or the Obligors which is permitted under the terms and conditions of the Bonds, may materially affect the ability of Anglian Water, the Issuer or the Obligors to pay amounts due and owing in respect of the Bonds.

## **6.7 Outsourcing Considerations**

As described in Chapter 4 under “*Anglian Water Business Description*”, Anglian Water has now discontinued its competitive tendering and outsourcing programme as it considers that current outsourcing levels are sufficient to deliver continued strong financial and operational performance.

## **6.8 Financial Ratios**

The Common Terms Agreement allows Anglian Water (following a Periodic Review or any material change in the regulation of the water industry in the United Kingdom) to amend any financial ratio contained within the covenants, Trigger Events or Events of Default provided that each Financial Guarantor and the Security Trustee (acting on the instructions of the Majority Creditors) agree and the Rating Requirements have been met.

## **6.9 Issuer and Bond Considerations**

### **6.9.1 Special Purpose Vehicle Issuer**

The Issuer is a special purpose financing entity with no business operations other than the incurrance of financial indebtedness, including the issuance of Bonds, entering into certain Authorised Credit Facilities and lending the proceeds of such financial indebtedness to Anglian Water under the Intercompany Loan Arrangements. The Issuer’s principal source of funds will be the funds available to it pursuant to the Authorised Credit Facilities and payments made to it by Anglian Water pursuant to the Intercompany Loan Arrangements. Therefore, the Issuer is, insofar as concerns the Intercompany Loan Arrangements, subject to all the restrictions relating to revenues to which Anglian Water is subject. Such restrictions could limit funds available to Anglian Water to enable it to satisfy in full and on a timely basis its obligations under the Intercompany Loan Arrangements and/or guarantee under the Security Agreement.

### **6.9.2 Bondholder rights subject to STID**

The Bonds are subject to the provisions of the STID. The STID contains provisions enabling the Security Trustee to implement various modifications, consents and waivers in relation to the Finance Documents and the Bonds, subject to Entrenched Rights and Reserved Matters. See Section 7.3.18, “*Financing Structure – Security Trust and Intercreditor Deed – Entrenched Rights and Reserved Matters*” below. The Security Trustee is authorised to act on the instructions of the Class A DIG, or following repayment of the Class A Debt, the Class B DIG. A Bondholder (other than (i) a USPP Bondholder holding a certain amount of Class A or Class B USPP Bonds prior to the occurrence of certain events; or (ii) after the occurrence of such events, any holder of USPP Bonds, as the case may be) will not be entitled to vote.

Prior to a Default Situation, the Bond Trustee may vote on behalf of the Unwrapped Bondholders (other than the USPP Bondholders) and (if an FG Event of Default has occurred and is continuing) the Wrapped Bondholders as part of the Instructing Group. However, the Bond Trustee will not be obliged to vote and will not be entitled to convene a meeting of Bondholders to seek directions in respect of such vote. Accordingly, subject to Entrenched Rights and Reserved Matters of the Bondholders, prior to a Default Situation, the Outstanding Principal Amount of the Wrapped Bonds (following the occurrence of an FG Event of Default) and the Unwrapped Bonds (other than the USPP Bonds) will not be voted as part of the Class A DIG or Class B DIG, as the case may be, in circumstances where the Bond Trustee is unable or unwilling to exercise its discretion.

During a Default Situation the Bond Trustee shall be entitled to vote and will be entitled to seek directions from the relevant Bondholders in respect of such vote. However, the Bond Trustee may be prevented from voting if a valid Emergency Instruction Notice is delivered to the Security Trustee. See Section 7.3.9, “*Emergency Instruction Procedure*”. In respect of a vote relating to Entrenched Rights and Reserved Matters, the Bond Trustee will be required to seek directions from the Bondholders of each affected Series of Bonds in respect of such vote.

Accordingly, subject to the Entrenched Rights and Reserved Matters of the Bondholders, decisions relating to and binding upon the Bonds may be made by persons with no interest in the Bonds and

the Bondholders may be adversely affected as a result. See Section 7.3, “*Financing Structure – Security Trust and Intercreditor Deed*”.

Under the terms of the STID and the CTA any further issues of debt securities by members of the Anglian Water Services Financing Group must be made subject to the intercreditor arrangements contained in the CTA and the STID (to which the Bonds are also subject). No alteration of the rights of priority of the holders of Class A Bonds, or, as the case may be, the Class B Bonds may be made without the consent of the relevant Bondholders.

### **6.9.3 Financial Guarantee**

Where applicable, a Financial Guarantor will guarantee to the relevant Class A Wrapped Bondholders and Class B Wrapped Bondholders only the payment of scheduled principal and interest of those Wrapped Bonds it has guaranteed; it will not guarantee the FG Excepted Amounts.

### **6.9.4 Limited Liquidity of the Bonds; Absence of Secondary Market for the Bonds**

Notwithstanding the fact that an application has been made for the Bonds to be admitted to the Official List and for such Bonds to be admitted to trading on the Market, there is currently no market for the Bonds. There can be no assurance that a secondary market will develop, or, if a secondary market does develop for any of the Bonds, that it will provide the holder of the Bonds with liquidity or that any such liquidity will continue for the life of the Bonds. Consequently, any purchaser of the Bonds must be prepared to hold such Bonds for an indefinite period of time or until final redemption or maturity of the Bonds.

The liquidity and market value at any time of the Bonds is affected by, among other things, the market view of the credit risk of such Bonds and will generally fluctuate with general interest rate fluctuations, general economic conditions, the condition of certain financial markets, international political events, the performance and financial condition of Anglian Water, developments and trends in the water industry generally and events in Anglian Water’s water supply and sewerage licence areas.

### **6.9.5 Rating of the Bonds**

The ratings assigned to the Class A Wrapped Bonds issued on the Effective Date were based solely on the debt rating of MBIA and reflect only the views of the Rating Agencies. The ratings assigned to all other Class A Wrapped Bonds and Class B Wrapped Bonds are based solely on the debt rating of the relevant Financial Guarantor and reflect only the views of the Rating Agencies. The ratings assigned to the Class A Unwrapped Bonds and the Class B Unwrapped Bonds by the Rating Agencies reflect only the views of the Rating Agencies.

**A rating is not a recommendation to buy, sell or hold securities and will depend, amongst other things, on certain underlying characteristics of the business and financial condition of Anglian Water or, in the case of the Class A Wrapped Bonds and/or Class B Wrapped Bonds of MBIA and/or any other Financial Guarantor from time to time.**

There is no assurance that any such ratings will continue for any period of time or that they will not be reviewed, revised, suspended or withdrawn entirely by the Rating Agencies (or any of them) as a result of changes in, or unavailability of, information or if, in the Rating Agencies’ judgement, circumstances so warrant. If any rating assigned to the Bonds is lowered or withdrawn, the market value of the Bonds may be reduced. Future events, including events affecting Anglian Water and/or circumstances relating to the water industry generally, could have an adverse impact on the ratings of the Bonds.

Where any Rating Agency is requested to confirm the then current ratings of the Bonds, or the shadow ratings of the Wrapped Bonds, or to confirm that such ratings or shadow ratings will not be downgraded following any particular event, or that a particular act or omission meets certain criteria of the Rating Agency, such confirmation may or may not be given at the sole discretion of the Rating Agency. Furthermore, it may not be possible or practicable for the Rating Agency to give such confirmation or to do so within any particular time period.

Confirmation, if and when given, will be given on the basis of the facts and circumstances prevailing at the relevant time, and in the context of cumulative changes to the transactions contemplated under the Programme since the Effective Date.

No assurance can be given that a requirement to seek any such confirmation from a Rating Agency will not have a subsequent impact upon the business of any member of the Anglian Water Services Financing Group.

A confirmation of ratings represents only a restatement of the opinions given at the Effective Date, and cannot be construed as advice for the benefit of any parties to the transactions contemplated under the Programme.

#### **6.9.6 Withholding Tax**

Unless otherwise specified in the applicable Final Terms, in the event withholding taxes are imposed by or in any jurisdiction in respect of payments due under the Bonds, the Issuer is not obliged to gross-up or otherwise compensate Bondholders for the fact that the Bondholders will receive, as a result of the imposition of such withholding taxes, cash amounts which are less than those which would otherwise have been the case. The Issuer will, in such event, have the option (but not the obligation) of: (i) redeeming all outstanding Bonds in full; (ii) arranging for the substitution of another company in an alternative jurisdiction (subject to certain conditions); or (iii) taking such other appropriate action as is reasonable to mitigate such tax. See Chapter 9, “*Terms and Conditions of the Bonds*”.

Likewise, in the event withholding taxes are imposed in respect of payments due under the Wrapped Bonds and MBIA and/or any other Financial Guarantor is called upon under any Bond Policy to make payments in respect of such payments, neither MBIA nor such other Financial Guarantor is obliged to gross-up or otherwise compensate Wrapped Bondholders for the fact that such Wrapped Bondholders will receive, as a result of the imposition of such withholding taxes, cash amounts which are less than those which would otherwise have been the case.

#### **6.9.7 Change of Law**

The structure of the transaction and, *inter alia*, the issue of the Bonds and ratings assigned to the Bonds are based on law, tax and administrative practice in effect at the date hereof, and having due regard to the expected tax treatment of all relevant entities under such law, tax and administrative practice. No assurance can be given that there will not be any change to such law, tax or administrative practice after the date hereof which change might impact on the Bonds and the expected payments of interest and repayment of principal.

#### **6.9.8 European Monetary Union**

Prior to the maturity of the Bonds, the UK may become a participating member state in the Economic and Monetary Union and the euro may become the lawful currency of the UK. Adoption of the euro by the UK may have the following consequences: (i) all amounts payable in respect of the Sterling denominated Bonds may become payable in euro; (ii) the introduction of the euro as the lawful currency of the United Kingdom may result in the disappearance of published or displayed rates for deposits in sterling used to determine the rates of interest on the Bonds or changes in the way those rates are calculated, quoted and published or displayed; and (iii) the Issuer may choose to redenominate the Bonds into euro and take additional measures in respect of the Bonds. The introduction of the euro could also be accompanied by a volatile interest rate. It cannot be said with certainty what effect, if any, adoption of the euro by the United Kingdom will have on investors in the Bonds.

#### **6.9.9 Hedging Risks**

The Issuer may be left exposed to interest rate risk or currency risk in the event that there is an early termination of a Hedging Agreement. A Hedging Agreement may be terminated in the circumstances described in Section 7.10, “Hedging Agreements”. If a Hedging Agreement is terminated and the Issuer is unable to find a replacement Hedge Counterparty, then the funds available to the Issuer may be insufficient to meet fully its obligations under the Bonds.

#### **6.9.10 Subordination of Class B Bonds**

The Class A Bonds and other Class A Debt rank and any further Class A Bonds and other Class A Debt will rank in priority to payments of principal and interest due on all Series of the Class B Bonds.

If, on any Interest Payment Date, prior to delivery of an Enforcement Notice, there are insufficient funds available to pay accrued interest on the Class B Bonds the Issuer's liability to pay such accrued interest will be treated as not having fallen due and will be deferred until the earlier of (i) the next following Interest Payment Date on which the Issuer has, in accordance with the cash management provisions of the CTA, sufficient funds available to pay such deferred amounts (including any interest accrued thereon); and (ii) the date upon which all Class A Debt has been paid in full. Interest will, however, accrue on such deferred interest.

Notwithstanding the subordination of, and credit enhancement provided by, the Class B Bonds to the Class A Debt the Issuer may optionally redeem some or all of the Class B Bonds provided that the original issue ratings assigned by any two of the Rating Agencies rating the Class A Bonds and the Class B Bonds would not be adversely affected.

It should be noted that all of the Payment Dates for the various different types of Class A Debt and Class B Debt do not and will not necessarily coincide and that, until a Standstill Period has commenced, there is no obligation to ensure that a payment made to a Class B Bondholder pursuant to the Bond Trust Deed (or any other Class B Debt Provider pursuant to any other Class B Debt) will not lead to a deficiency of funds to make payments in respect of Class A Debt that fall due on a later date.

#### **6.9.11 Tax Consequences Of The Introduction Of International Financial Reporting Standards**

For accounting periods beginning on or after 1 January, 2005 the accounts of the Issuer (being a United Kingdom company with listed debt) are required to comply either with International Financial Reporting Standards (“**IFRS**”) or with new UK Financial Reporting Standards (“**new UK FRS**”) which are based on IFRS. (In the following, unless otherwise stated, references to IFRS include references to new UK FRS). Accordingly, the Issuer is required to apply IFRS from the start of its accounting period beginning on 1 April 2005. It is not clear whether the tax position of the Issuer will be the same under IFRS as it was under U.K. GAAP as it applied for the Issuer's previous accounting periods up to 31 March 2004 (“**old U.K. GAAP**”). HM Revenue & Customs have indicated that, as a policy matter, they do not wish the tax neutrality of securitisation special purpose companies (such as the Issuer) to be disrupted as a result of the transition to IFRS and that they are willing to work with the industry to identify appropriate means of preventing such disruption.

As a first step, the Finance Act 2005 contains legislation creating a special interim corporation tax regime for “securitisation companies”. The effect of this legislation is to allow securitisation companies to prepare tax computations on the basis of old U.K. GAAP as applicable up to 31 December, 2004 for all accounting periods beginning on or after 1 January, 2005 and ending before 1 January, 2007, notwithstanding any requirement to prepare statutory accounts under IFRS. The Finance Act 2005 also contains a power to make regulations to establish a permanent regime for securitisation special purpose vehicles.

The Issuer will qualify as a “securitisation company” for the purposes of the interim regime. This should allow the Issuer to avoid any impact of IFRS on its tax computations for any accounting period ending before 1 January, 2007. Further, provided that HM Revenue & Customs adhere to the policy objectives that they have indicated in this area and which are have confirmed in Budget Notice REV 13, it is expected that secondary legislation will be put in place pursuant to enabling legislation in the Finance Act 2005 to ensure that the taxation treatment of companies such as the Issuer does not change as a result of the introduction of IFRS so as to give rise to any incremental unfunded tax liabilities. There is, however, no certainty that such secondary legislation will be introduced or, if it is introduced, that it will extend to the Issuer.

#### **6.10 Catastrophe Risk**

Catastrophic events such as dam bursts, fires, earthquakes, floods, droughts, terrorist attacks, diseases, plant failure or other similar events could result in personal injury, loss of life, pollution or environmental

damage, severe damage or destruction of Anglian Water's water or sewage treatment works, pumping stations, water mains, sewers or service pipes. Any resulting damage or suspension of operations of Anglian Water, to the extent not covered by insurance, could have a material adverse impact on the ability of Anglian Water to meet its financing and regulatory obligations.

**The Issuer believes that the risks described above are the principal risks inherent in the Programme. However, the inability of the Issuer to pay interest or repay principal on the Bonds, or the ability of any Financial Guarantor to pay scheduled interest or repay scheduled principal on the Class A Wrapped Bonds and/or the Class B Wrapped Bonds, may occur for other reasons, and the Issuer does not represent that the above statements of the risks of holding the Bonds are exhaustive. While the various structural elements described in this document are intended to lessen some of these risks for holders of the Bonds, there can be no assurance that these measures will ensure that the holders of the Bonds receive payment of interest or repayment of principal from the Issuer in respect of such Bonds, or from any Financial Guarantor in respect of the Class A Wrapped Bonds and/or the Class B Wrapped Bonds on a timely basis or at all.**



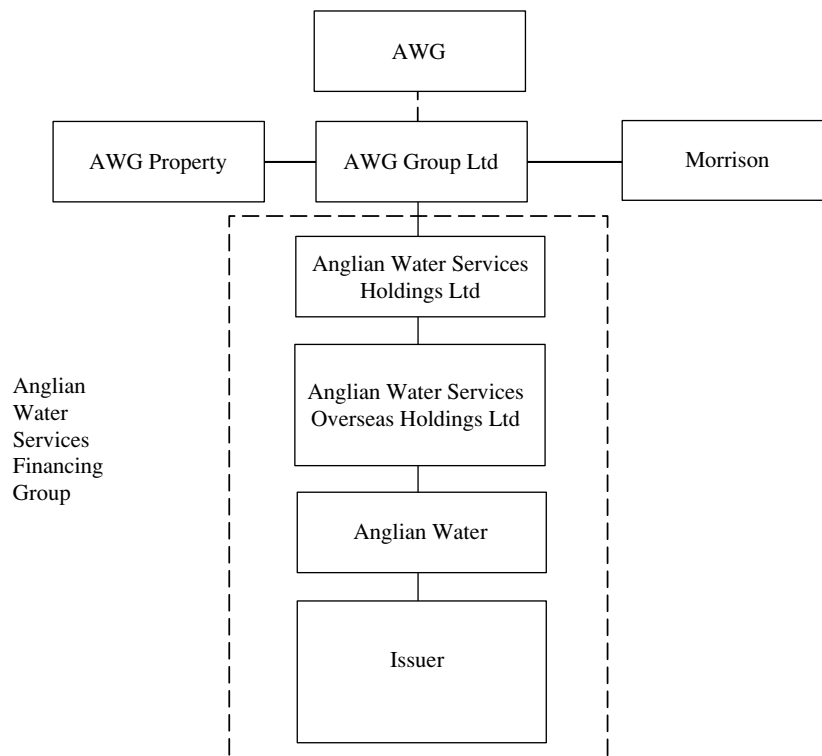
## CHAPTER 7

### FINANCING STRUCTURE

#### 7.1 The Anglian Water Services Financing Group

In 2002 AWG implemented a significant corporate restructuring and financing through the creation of the new Anglian Water Services Financing Group within the AWG Group. The Anglian Water Services Financing Group consists of Anglian Water Services Holdings Ltd, Anglian Water Services Holdings Ltd's wholly-owned subsidiary, Anglian Water Services Overseas Holdings Ltd, Anglian Water Services Overseas Holdings Ltd's wholly-owned subsidiary, Anglian Water and Anglian Water's wholly-owned subsidiary, Anglian Water Services Financing plc (see diagram, "*Ownership Structure of Anglian Water Services Financing Group*" below). The creation of the Anglian Water Services Financing Group within the AWG Group facilitated the financing of Anglian Water through, *inter alia*, the issuance of Bonds and other financial indebtedness incurred by the Issuer. AWG Group Ltd's and/or Anglian Water's obligations under the Existing Bonds and the Transferred USPP Bonds (and the rights and obligations under Hedging Agreements hedging those Bonds) were transferred to the Issuer in return for the granting by Anglian Water of loan notes in favour of the Issuer and the assignment to the Issuer and the amendment of certain existing intercompany loans. Further, the Issuer has been, and will continue to be, funded by proceeds of Bonds issued under the Programme and other financial indebtedness. This is lent by the Issuer to Anglian Water pursuant to the Issuer/Anglian Water Loan Agreement (see 7.4, "*Intercompany Loan Arrangements*" below). Anglian Water on-lent certain of the monies borrowed by it from the Issuer to Anglian Water Services Holdings Ltd pursuant to an interest-bearing loan and Anglian Water Services Holdings Ltd used the proceeds of the borrowings to satisfy its obligations to pay to AWG Group Ltd the consideration for the acquisition by it of shares in Anglian Water Services Overseas Holdings Ltd.

#### Ownership Structure of Anglian Water Services Financing Group



## 7.2 Sources of Funds and Debt Transfer

### 7.2.1 Sources of funds

At the date of this Prospectus, the Issuer has available to it financial accommodation from the following sources:

- (i) the Bonds issued for cash;
- (ii) the Authorised Loan Facility;
- (iii) the Hedging Agreements;
- (iv) the Debt Service Reserve Liquidity Facilities; and
- (v) the O&M Reserve Facility.

The Issuer is also permitted, subject to the terms of the Common Terms Agreement to incur additional Permitted Financial Indebtedness including issuing Bonds under the Programme and such additional Permitted Financial Indebtedness may either be secured Class A Debt or Class B Debt (provided the lender accedes to the CTA and STID) (see 7.3, “*Security Trust and Intercreditor Deed*” and 7.5, “*Common Terms Agreement*”).

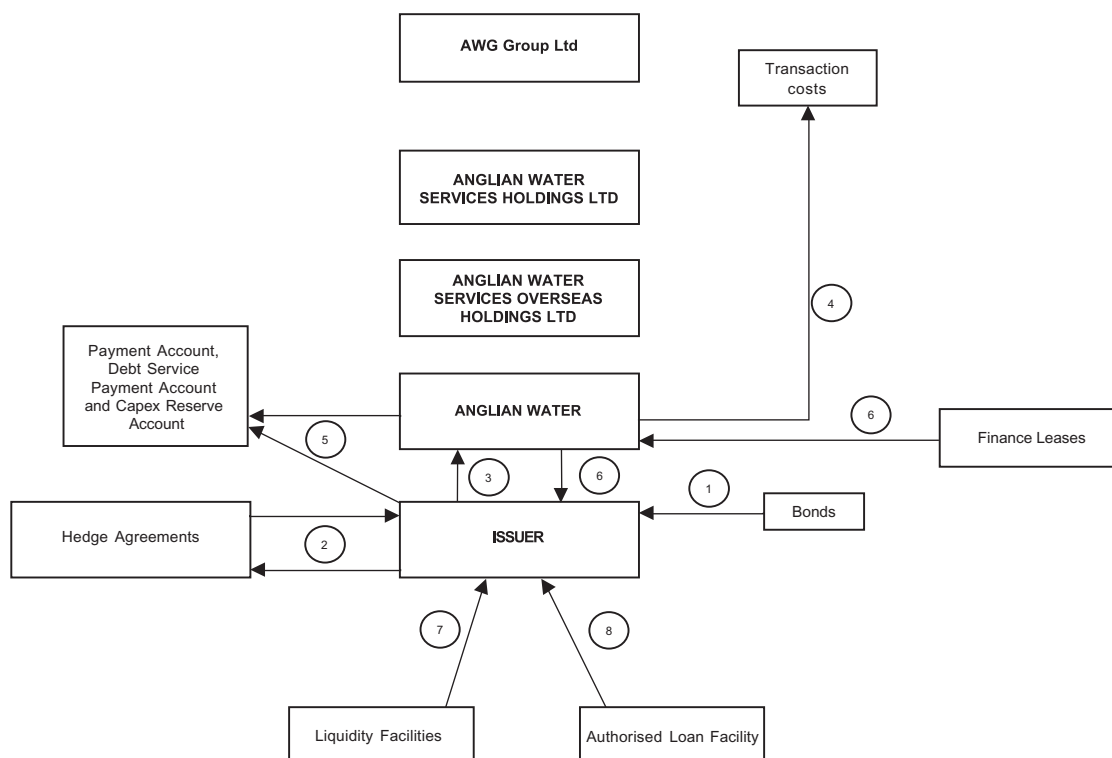
The Issuer may also (subject to the terms of the CTA) enter into certain unsecured financing arrangements.

All monies borrowed by the Issuer have been, and will be, automatically on-lent to Anglian Water under the Intercompany Loan Arrangements (see 7.4, “*Intercompany Loan Arrangements*”). The Intercompany Loan Arrangements provide for payments to become due from Anglian Water to the Issuer on dates and in amounts that match the obligations of the Issuer to its various financiers under its financial arrangements plus a management fee. To further reinforce the ability of the income of Anglian Water to be utilised in repayment of the Issuer’s debt, Anglian Water has guaranteed the obligations of the Issuer to the Secured Creditors and has executed a Security Agreement in favour of the Security Trustee to secure its obligations under that guarantee (see 7.7, “*Security Agreement*”).

The financial accommodation available to the Anglian Water Services Financing Group also includes Finance Leases which are available to Anglian Water. The purpose of the guarantee referred to above and the provisions of the STID are, *inter alia*, to prevent any structural subordination of other Secured Creditors to the Finance Lessors that may otherwise result.

Hedging arrangements have been entered into by the Issuer and the effect of these are passed on to Anglian Water via the Intercompany Loan Arrangements (see 7.4, “*Intercompany Loan Arrangements*”).

## 7.2.2 Cashflow and Debt Structure on an Issue Date



### Notes:

The steps described below all relate to the cashflow and debt structure of the Anglian Water Services Financing Group on an Issue Date:

1. receive net proceeds of new Bonds issued for cash on the relevant Issue Date;
2. swap any proceeds received in a currency (other than Sterling) for Sterling;
3. loan the proceeds of the new Bonds to Anglian Water under the Issuer/Anglian Water Loan Agreement;
4. pay fees and other costs associated with the issue of the new Bonds;
5. payments into the Payment Account and Capex Reserve Account of Anglian Water and the Debt Service Payment Account of the Issuer;
6. Finance Leases remain with Anglian Water subject to the provisions of the CTA and STID;
7. Debt Service Reserve Liquidity Facilities and O&M Reserve Facility made available to the Issuer for debt service and certain operating and maintenance expenditure requirements; and
8. Authorised Loan Facility made available to the Issuer for working capital and capital expenditure requirements.

## 7.2.3 Debt Transfer

On the Effective Date the Issuer was substituted as the issuer in respect of the Existing Bonds (previously issued by AWG Group Ltd pursuant to the Existing Bond Trust Deeds) pursuant to a prior consent solicitation of the holders of such Existing Bonds. In addition the Issuer issued the Transferred USPP Bonds (other than the USPP 2001 Bonds) under the Programme to the relevant holders thereof in exchange for the related bonds held by such holders and previously issued by AWG Group Ltd, pursuant to exchange agreements entered into between the Issuer, AWG Group Ltd and such holders on or around the Effective Date. The Issuer also assumed, pursuant to an assumption agreement executed in accordance with the terms of the Note Purchase Agreement, all the obligations of Anglian Water in respect of the USPP 2001 Bonds. The consideration for the assumption by the Issuer of the primary obligations under the Existing Bonds, the Transferred USPP Bonds, and the related Hedging Agreements was the issue by Anglian Water to the Issuer of the loan notes and the assignment to the Issuer and amendment of certain existing intercompany loans (Anglian Water having been simultaneously released by AWG Group Ltd from intercompany indebtedness in an amount corresponding to such Existing Bonds and Transferred USPP Bonds (other than the USPP 2001 Bonds)) (see 7.4.1, “*Anglian Water Loan Notes*”).

## 7.3 Security Trust and Intercreditor Deed

### 7.3.1 General

The intercreditor arrangements in respect of the Anglian Water Services Financing Group (the “**Intercreditor Arrangements**”) are contained in the STID and the CTA. The Intercreditor Arrangements bind each of the Secured Creditors and each of the Obligors.

The Secured Creditors include the Class A Debt Providers and the Class B Debt Providers. Any new Authorised Credit Provider (or in respect of Bondholders (other than holders of the USPP 2001 Bonds), the Bond Trustee) is required to accede to the STID and the CTA as a Class A Debt Provider or a Class B Debt Provider. The Local Authority Loan is not subject to the Intercreditor Arrangements.

Unsecured creditors have not and will not become parties to the Intercreditor Arrangements and although ranking behind the Secured Creditors in an administration or other enforcement will have unfettered, independent rights of action in respect of their debts. However, the aggregate amount of unsecured debt is restricted to levels acceptable to the Secured Creditors. See 7.5, “*Common Terms Agreement*”.

The purpose of the Intercreditor Arrangements is to regulate, *inter alia*: (i) the claims of the Secured Creditors; (ii) the exercise, acceleration and enforcement of rights by the Secured Creditors; (iii) the rights of the Secured Creditors to instruct the Security Trustee; (iv) the rights of the Secured Creditors during a Standstill Period (see 7.3.13, “*Standstill*” below); (v) the Entrenched Rights and the Reserved Matters of the Secured Creditors; and (vi) the giving of consents and waivers and the making of modifications to the Finance Documents.

The Intercreditor Arrangements provide for the ranking in point of payment of the claims of the Secured Creditors and for the subordination of all intra Anglian Water Services Financing Group claims (other than claims in respect of the Intercompany Loan Arrangements).

### 7.3.2 Undertakings of Secured Creditors

Pursuant to the terms of the STID, each Secured Creditor (other than the Security Trustee and the Bond Trustee) undertakes that it will not, unless the Majority Creditors otherwise agree:

- (i) permit or require any Obligor to discharge any of the Secured Liabilities owed to it, save to the extent permitted by the CTA and the STID;
- (ii) permit or require any Obligor to pay, prepay, repay, redeem, purchase, early or voluntarily terminate or otherwise acquire any of the Secured Liabilities owed to it, save to the extent permitted by the CTA and the STID;
- (iii) take, accept or receive the benefit of any security interest, guarantee, indemnity or other assurance against financial loss from any of the Obligors in respect of any of the Secured Liabilities owed to it, except the Security and the Bond Policies or pursuant to the terms of the Finance Documents;
- (iv) take or receive from any of the Obligors by cash receipt, set-off, any right of combination of accounts or in any other manner whatsoever, the whole or any part of the Secured Liabilities owed to it, save to the extent permitted by the CTA and the STID; or
- (v) except as described in 7.3.5, “*Modifications, Consents and Waivers*” below, agree to any modification to, or consent or waiver under or in respect of, the Finance Documents to which it is a party.

### 7.3.3 Undertakings of Obligors

- (i) Pursuant to the terms of the STID, each Obligor undertakes that it will not, unless the Majority Creditors otherwise agree:
  - (a) discharge any of the Secured Liabilities owed by it, save to the extent permitted by the CTA and the STID;

- (b) pay, prepay, repay, redeem, purchase, early or voluntarily terminate or otherwise acquire any of the Secured Liabilities owed by it, save to the extent permitted by the CTA and the STID;
  - (c) create or permit to subsist any Security Interest over any of its assets for, or any guarantee, indemnity or other assurance against financial loss in respect of, any of the Secured Liabilities owed by it, except the Security and the Bond Policies or pursuant to the terms of the Finance Documents;
  - (d) discharge any of the Secured Liabilities by cash payment, set-off, any right of combination of accounts or in any other manner whatsoever, save to the extent permitted by the CTA and the STID;
  - (e) without the consent of the Security Trustee or, where applicable, each relevant Secured Creditor (as described in 7.3.5, “*Modifications, Consents and Waivers*” below), agree to any modification to, or consent or waiver under or in respect of, any term of any Finance Document to which it is a party; or
  - (f) take or omit to take any action whereby any subordination contemplated by the STID may be impaired.
- (ii) In addition, pursuant to the terms of the STID, each Obligor undertakes that it will not until all the Secured Liabilities have been discharged in full, unless the Majority Creditors otherwise agree:
- (a) discharge any of the Subordinated Liabilities owed by it or require any other Obligor to discharge any of the Subordinated Liabilities owed to it, save to the extent permitted by the CTA and the STID;
  - (b) pay, prepay, repay, redeem or make any distribution in respect of, or purchase or acquire, any of the Subordinated Liabilities owed by it or permit any other Obligor to do so in respect of any of the Subordinated Liabilities owed to it;
  - (c) create or permit to subsist any Security Interest over any of its assets for, or any guarantee, indemnity or other assurance against financial loss in respect of, any of the Subordinated Liabilities owed by it or take, accept or receive the benefit of any Security Interest for, or any guarantee, indemnity or other assurance against financial loss in respect of, any of the Subordinated Liabilities owed to it;
  - (d) discharge any of the Subordinated Liabilities owed by it by cash payment, set-off, any right of combination of accounts or in any other manner whatsoever or take or receive from, or permit the discharge by, any of the Obligors by cash receipt, set-off or in any other manner whatsoever, the whole or any part of the Subordinated Liabilities owed to it; or
  - (e) take or omit to take any action whereby the subordination contemplated by the STID may be impaired.

The Obligors are (unless the Security Trustee directs otherwise) entitled without Majority Creditor consent to pay any scheduled amounts due and payable pursuant to the terms of the UK Holdco/Anglian Water Loan and/or the Intercompany Loan Arrangements.

#### **7.3.4 Ranking of Secured Liabilities**

The underlying principle of the Intercreditor Arrangements is that the Class A Debt ranks in point of payment prior to any payment in respect of the Class B Debt at all times (including both prior to and during any Standstill Period, after acceleration of the Secured Liabilities and upon any enforcement of the Security). Prior to a Standstill Period payment dates for Class A Debt and Class B Debt may fall on different dates.

### 7.3.5 Modifications, Consents and Waivers

Subject to the Entrenched Rights and Reserved Matters (see 7.3.18, “*Entrenched Rights and Reserved Matters*”), the Security Trustee shall only agree to any modification of or grant any consent or waiver under the Finance Documents or (subject to restrictions during a Standstill Period) take Enforcement Action with the consent of or if so instructed by the Majority Creditors. Not all proposals which require the consent of the Majority Creditors will be sent to all Secured Creditors (or their Secured Creditor Representatives, as the case may be). In certain circumstances, the Security Trustee is authorised to consult with the DIG Representatives only.

Subject to the Entrenched Rights and Reserved Matters (see 7.3.18, “*Entrenched Rights and Reserved Matters*”), the Security Trustee may make modifications to the Finance Documents without the consent of any other Secured Creditor if such modifications are to correct manifest errors or are of a formal, minor or technical nature.

### 7.3.6 Class A Debt Instructing Group

Both prior to and during any Standstill Period, after acceleration of the Secured Liabilities and upon any enforcement of the Security, only the Qualifying Class A Debt Providers will be eligible to exercise the rights of the Majority Creditors. Prior to repayment in full of the Class A Debt, decisions of such Majority Creditors will bind all of the Secured Creditors in all circumstances, save for certain Entrenched Rights and Reserved Matters that are fundamental to particular Secured Creditors (see 7.3.18, “*Entrenched Rights and Reserved Matters*” below).

The Qualifying Class A Debt Providers will exercise their rights through the following representatives which will together be entitled to vote on certain proposals as part of the “**Class A Debt Instructing Group**” or the “**Class A DIG**”. The Class A DIG will be comprised of the following representatives (each, a “**Class A DIG Representative**”):

- (i) in respect of each Series of Class A Wrapped Bonds (if no FG Event of Default has occurred and is continuing), the Financial Guarantor;
- (ii) in respect of each Series of Class A Wrapped Bonds (after an FG Event of Default has occurred and is continuing in respect of the Financial Guarantor of those Class A Wrapped Bonds) and each Series of Class A Unwrapped Bonds (other than USPP Bonds), the Bond Trustee;
- (iii) in respect of Class A USPP Bonds, (a) prior to the occurrence of an Event of Default, any USPP Bondholder who has outstanding to it or any of its affiliates more than US\$70,000,000 of Class A USPP Bonds or (b) after an Event of Default has occurred and is continuing, any USPP Bondholder;
- (iv) in respect of tranche A1 and tranche B and the Class A portion of tranche A2 of a bridge facility (the “**Bridging Facility**”) provided by Barclays Bank PLC and Citibank, N.A. (the “**Original Lenders**”) which has now been cancelled in its entirety, Barclays Bank PLC as bridging facility agent (the “**Bridging Facility Agent**”);
- (v) in respect of the Initial Authorised Loan Agreement, the Initial Authorised Credit Facility Agent;
- (vi) in respect of any Existing Finance Leases, the relevant Finance Lessor; and
- (vii) in respect of any other Secured Liabilities of the type referred to in paragraphs (i) to (vi) above or (with the approval of the Majority Creditors) other types of Secured Liabilities that rank *pari passu* with all other Class A Debt, the relevant representative appointed under the terms of the relevant Finance Document and named in the relevant Accession Memorandum to the STID and the CTA as the Class A DIG Representative.

Each Class A DIG Representative will be required to provide an indemnity to the Security Trustee each time it votes as part of the Class A DIG irrespective of whether it is a Majority Creditor.

Unless a Default Situation has occurred and is continuing, the Bond Trustee shall not be entitled to convene a meeting of any Series of Bonds to consider any proposal to be voted on by the Class A DIG.

Decisions of the Majority Creditors will be determined by votes on a pound for pound basis (based on the Outstanding Principal Amount of the Qualifying Class A Debt voted by the Class A DIG Representatives). Subject to Entrenched Rights and Reserved Matters, the Security Trustee will be entitled to act on the instructions of the Majority Creditors of those Class A DIG Representatives which have actually voted by the specified date for voting which must be not less than 10 business days (or in certain circumstances 5 business days) (or, where the Bond Trustee is a DIG Representative and a Default Situation is continuing (subject to the Emergency Instruction Procedure – see 7.3.9, “*Emergency Instruction Procedure*” below), such later date (not later than 2 months after such date) as is requested of the Security Trustee by the Bond Trustee should the Bond Trustee consider it necessary to convene a meeting of any one or more Series of Bondholders to seek directions) or, if earlier, as soon as Class A DIG Representatives in respect of more than 50 per cent. of the Qualifying Class A Debt have voted in favour of the relevant proposal.

### 7.3.7 Class B Debt Instructing Group

Following repayment in full of the Class A Debt, the Qualifying Class B Debt Providers will be eligible to exercise the rights of the Majority Creditors. After repayment in full of the Class A Debt, decisions of such Majority Creditors will bind all of the Secured Creditors in all circumstances, save for certain Entrenched Rights and Reserved Matters that are fundamental to particular Secured Creditors. See 7.3.18, “*Entrenched Rights and Reserved Matters*”.

The Qualifying Class B Debt Providers will exercise their rights through a group of representatives which will together be entitled to vote on certain proposals as part of the “**Class B Debt Instructing Group**” or the “**Class B DIG**”. The Class B DIG will be comprised of the following representatives (each, a “**Class B DIG Representative**”):

- (i) in respect of each Series of Class B Wrapped Bonds (if no FG Event of Default has occurred and is continuing), the Financial Guarantor;
- (ii) in respect of each Series of Class B Wrapped Bonds (after an FG Event of Default has occurred and is continuing in respect of the Financial Guarantor of those Class B Wrapped Bonds) and each Series of Class B Unwrapped Bonds, the Bond Trustee;
- (iii) in respect of the Class B portion of tranche A2 of the Bridging Facility, the Bridging Facility Agent; and
- (iv) in respect of any other Secured Liabilities of the type referred to in paragraphs (i) to (iii) above or (with the approval of the Majority Creditors) other types of Secured Liabilities that rank *pari passu* with all other Class B Debt, the relevant representative appointed under the terms of the relevant Finance Document and named in the relevant Accession Memorandum as the Class B DIG Representative.

Each Class B DIG Representative will be required to provide an indemnity to the Security Trustee each time it votes as part of the Class B DIG irrespective of whether it is a Majority Creditor.

Unless a Default Situation has occurred and is continuing, the Bond Trustee shall not be entitled to convene a meeting of any Series of Bonds to consider any proposal to be voted on by the Class B DIG.

Decisions of the Majority Creditors will be determined by votes on a pound for pound basis (based on the Outstanding Principal Amount of the Qualifying Class B Debt voted by the Class B DIG Representatives). Subject to Entrenched Rights and Reserved Matters, the Security Trustee will be entitled to act on the instructions of the Majority Creditors of those Class B DIG Representatives which have actually voted by the specified date for voting which must be not less than 10 business days (or in certain circumstances 5 business days) (or, where the Bond Trustee is a DIG Representative and a Default Situation is continuing (subject to the Emergency Instruction Procedure – see 7.3.9, “*Emergency Instruction Procedure*” below), such later date (not later than

2 months after such date) as is requested of the Security Trustee by the Bond Trustee should the Bond Trustee consider it necessary to convene a meeting of any one or more Series of Bondholders to seek directions) or, if earlier, as soon as Class B DIG Representatives in respect of more than 50 per cent. of the Qualifying Class B Debt have voted in favour of the relevant proposal.

### **7.3.8 Voting by the Bond Trustee as DIG Representative of the Bondholders**

Where the Bond Trustee acts as the DIG Representative of the Wrapped Bondholders (following the occurrence of an FG Event of Default which is continuing) and/or the Unwrapped Bondholders (other than the USPP Bondholders), the Bond Trustee may, both prior to a Default Situation and/or whilst a Default Situation is continuing, in its absolute discretion, vote on a STID Proposal or a DIG Proposal (without reference to any Bondholders) in respect of the total Outstanding Principal Amount of some or all such Series of Bonds), but shall not, prior to a Default Situation, be entitled to convene a meeting of Bondholders to seek directions.

Additionally, whilst a Default Situation is continuing, where the Bond Trustee acts as the DIG Representative in respect of the Bonds, the Bond Trustee:

- (i) subject to (ii) below, may, in its absolute discretion, direct the Security Trustee in respect of the total Outstanding Principal Amount of any Series of Wrapped Bonds (following the occurrence of an FG Event of Default in respect of the Financial Guarantor of such Series of Wrapped Bonds, which is continuing) and/or Unwrapped Bonds (other than USPP Bonds); and
- (ii) shall not be entitled to convene a meeting of the Bondholders to direct the Security Trustee in accordance with an extraordinary resolution of any such Series of Bonds after the presentation of a valid Emergency Instruction Notice pursuant to the terms of the STID. See 7.3.9, “*Emergency Instruction Procedure*” below.

### **7.3.9 Emergency Instruction Procedure**

Whilst a Default Situation is subsisting, certain decisions and instructions may be required in a timeframe which does not allow the Bond Trustee to convene Bondholder meetings. To cater for such circumstances, the Intercreditor Arrangements provide for an emergency instruction procedure (the “**Emergency Instruction Procedure**”) which is subject to Entrenched Rights and Reserved Matters. The Security Trustee will be required to act upon instructions contained in an emergency instruction notice (an “**Emergency Instruction Notice**”). An Emergency Instruction Notice must be signed by DIG Representatives (the “**EIN Signatories**”) representing 66% per cent. or more of the aggregate Outstanding Principal Amount of the Qualifying Class A Debt (or following the repayment in full of the Class A Debt, the Qualifying Class B Debt) after excluding the proportion of Qualifying Debt in respect of which the Bond Trustee is the DIG Representative and in respect of which the Bond Trustee in its absolute discretion has not voted. The Emergency Instruction Notice must specify the emergency action which the Security Trustee is being instructed to take and must certify that in their reasonable opinion, unless such action is taken within the timeframe specified in the Emergency Instruction Notice, the interests of the EIN Signatories will be materially prejudiced.

### **7.3.10 Hedge Counterparties**

Each Hedge Counterparty is a Secured Creditor party to the STID and each Hedging Agreement constitutes Class A Debt.

The Hedge Counterparties do not form part of the Class A DIG. However, the Hedge Counterparties will generally rank in the Payment Priorities senior to or *pari passu* with interest and principal payments on the Class A Bonds. See 7.6, “*Cash Management*” and 7.10, “*Hedging Agreements*”.

### **7.3.11 Liquidity Facility Providers**

Each Liquidity Facility Provider is a Secured Creditor party to the STID and each Liquidity Facility Agreement constitutes Class A Debt.



The Liquidity Facility Providers do not form part of the Class A DIG. However, the Liquidity Facility Providers will rank in the Payment Priorities senior to interest and principal payments on the Class A Bonds. See 7.6, “Cash Management” and 7.9.4, “The Liquidity Facilities”.

### 7.3.12 Finance Lessors

Each Finance Lessor is a Secured Creditor party to the STID and all amounts arising under the Finance Leases constitute Class A Debt.

Existing Finance Lessors will form part of the Class A DIG. Amounts due and payable under the Finance Leases are dealt with in 7.6, “Cash Management” and 7.9.1, “Existing Finance Leases”.

### 7.3.13 Standstill

The STID provides for an automatic standstill of the claims of the Secured Creditors against Anglian Water and the Issuer (the “Standstill”) immediately following notification to the Security Trustee of an Event of Default.

The Standstill is designed to reduce or postpone the likelihood of a Special Administration Order being made against Anglian Water on the grounds of its insolvency or otherwise. Although not binding on unsecured and trade creditors and hence potentially giving such unsecured and trade creditors a position of greater strength upon an Event of Default, it is intended to allow time for the Secured Creditors to restore the financial condition of Anglian Water.

During the Standstill Period:

- (i) other than any action taken in relation to Permitted Accelerations, none of the Secured Creditors will be entitled to give any instructions to the Security Trustee to take any Enforcement Action (but without prejudice to the ability of the Secured Creditors to demand payment) in relation to the Security granted by the Issuer or Anglian Water;
- (ii) the Security granted by Anglian Water Services Holdings Ltd and Anglian Water Services Overseas Holdings Ltd may be enforced at any time by the Security Trustee at the direction of the Majority Creditors;
- (iii) save as provided in sub-paragraphs (i) and (ii) above and other than Permitted Accelerations, no Enforcement Action may be taken;
- (iv) any monies received by Anglian Water or the Issuer will be applied in accordance with the cash management provisions contained in the CTA (see 7.6, “Cash Management” below) and in accordance with the Payments Priorities (see 7.6.5, “Cash Management – Debt Service Payment Account” below); and
- (v) the Secured Creditors will benefit from the Liquidity Facilities.

Notwithstanding the Standstill, the Secured Creditors are entitled to accelerate their claims to the extent required to apply proceeds of enforcement of the share pledges provided by Anglian Water Services Holdings Ltd and Anglian Water Services Overseas Holdings Ltd under the Security Documents and in the case of the Original Lenders to the extent required to apply the proceeds towards the Class B portion of the Bridging Facility.

The period of the Standstill (the “Standstill Period”) will be 18 months unless the Standstill Period is extended beyond 18 months (see 7.3.14, “Standstill Extension” below) or any of the following occur prior to the expiry of the relevant Standstill Period:

- (i) the date on which an order is made for the Special Administration of Anglian Water or any steps are taken to commence insolvency proceedings against any other Obligor other than proceedings that are commenced by the Security Trustee;
- (ii) (during the first 18 months of the Standstill Period) the date on which Class A DIG Representatives in respect of 66% per cent. or more of the aggregate Outstanding Principal Amount of the Qualifying Class A Debt or (following the repayment in full of the Class A Debt) Class B DIG Representatives in respect of 66% per cent. or more of the aggregate Outstanding Principal Amount of the Qualifying Class B Debt vote to terminate the

Standstill Period and (after the first 18 months) the date on which the Standstill Period terminates (see 7.3.14, “*Standstill Extension*” below);

- (iii) the date of waiver of the relevant Event of Default or the date of remedy of the Event of Default giving rise to the Standstill Period.

#### **7.3.14 Standstill Extension**

The Standstill Period shall automatically be extended beyond 18 months:

- (i) for a further 120 days unless Class A DIG Representatives in respect of 50 per cent. or more of the aggregate Outstanding Principal Amount of Qualifying Class A Debt vote at any time prior to or during such further 120 days to terminate the Standstill Period;
- (ii) following the period referred to in sub-paragraph (i), for a further 60 days unless Class A DIG Representatives in respect of 33% per cent. or more of the aggregate Outstanding Principal Amount of Qualifying Class A Debt vote at any time prior to or during such further 60 days to terminate the Standstill Period;
- (iii) following the period referred to in sub-paragraph (ii), for a further 60 days unless Class A DIG Representatives in respect of 10 per cent. or more of the aggregate Outstanding Principal Amount of Qualifying Class A Debt vote at any time prior to or during such further 60 days to terminate the Standstill Period; and
- (iv) following the period referred to in sub-paragraph (iii), for successive periods each of 60 days unless Class A DIG Representatives in respect of 10 per cent. or more of the aggregate Outstanding Principal Amount of Qualifying Class A Debt vote at any time prior to or during such further 60 days to terminate the Standstill Period and a vote shall be taken of the relevant Class A DIG Representatives on the expiry of each subsequent period of 60 days for so long as the Standstill Period continues as to whether the Standstill Period should continue for a further period of 60 days.

The Bond Trustee shall not form part of the Class A DIG in respect of any vote to terminate the Standstill Period, unless directed or requested to vote in such manner (i) by an Extraordinary Resolution of the relevant Series of Class A Bonds or (ii) in writing by Bondholders holding not less than the Outstanding Principal Amount of the relevant Series of Class A Bonds as specified in Condition 19(a) or the equivalent condition of the relevant Existing Bonds.

When the Class A Debt has been fully repaid, the rights to terminate the Standstill Period as described above shall be vested in the Class B DIG Representatives.

#### **7.3.15 Enforcement**

Subject to certain matters and to certain exceptions, following an enforcement, any proceeds of enforcement or other monies held by the Security Trustee under the STID will be applied by the Security Trustee in accordance with the Payment Priorities (see 7.6.5, “*Debt Service Payment Account*” below).

The Secured Creditors do not (with certain limited exceptions outlined in this Prospectus) have the right independently to accelerate their claims under their own facilities and agreements prior to termination of a Standstill Period. The Security Trustee will take all enforcement action and will be instructed by the Majority Creditors. Immediately upon notification to the Security Trustee of any Event of Default, the Standstill Period will commence, during which period no Secured Creditor may take any action to recover their debt or enforce the Security granted by Anglian Water or the Issuer. The Security granted by Anglian Water Services Holdings Ltd and Anglian Water Services Overseas Holdings Ltd may be enforced by the Security Trustee with the consent of the Majority Creditors as prescribed in the STID.

#### **7.3.16 Accession of Additional Secured Creditors**

The STID requires that, to the extent that Anglian Water and/or the Issuer wishes any Authorised Credit Provider (or in respect of Bonds, its Secured Creditor Representative) or other person to obtain the benefit of the Security, such Authorised Credit Provider or other person (other than

Bondholders (excluding holders of USPP 2001 Bonds)) must sign an Accession Memorandum whereby it agrees to be bound by the terms of the STID and the CTA, including those provisions which prohibit individual Secured Creditors from taking actions without the consent of the Majority Creditors.

### **7.3.17 Activities of the Security Trustee**

Subject to its Entrenched Rights and Reserved Matters and certain exceptions, the Security Trustee will only be required to take any action if instructed to do so by the Majority Creditors or, in particular cases, other specified parties and indemnified to its satisfaction.

Subject to certain exceptions, when granting any consent or waiver or exercising any power, trust, authority or discretion relating to or contained in the STID, the Finance Documents or any ancillary documents, the Security Trustee will act in accordance with its sole discretion (where granted such right) or as directed, requested or instructed by or subject to the agreement of the Majority Creditors or, in particular cases, other specified parties and in accordance with the provisions of the STID.

### **7.3.18 Entrenched Rights and Reserved Matters**

Modifications, consents and waivers will be agreed by the Security Trustee, in accordance with votes of the Majority Creditors, subject to Entrenched Rights and Reserved Matters. Such modifications, consents and waivers will be binding on all of the Secured Creditors, subject to Entrenched Rights and Reserved Matters. No Entrenched Right or Reserved Matter will operate to override the provisions contained in the CTA which allow Anglian Water (following a Periodic Review or as a result of any material change in the regulation of the water industry in the United Kingdom) to amend any financial ratio contained within the covenants, Trigger Events or Events of Default provided that each Financial Guarantor and the Security Trustee (acting on the instructions of the Majority Creditors) agree and the Rating Requirements have been met.

Lists of Entrenched Rights and Reserved Matters are contained in 7.3.19, “*Entrenched Rights*” and 7.3.20, “*Reserved Matters*”, below.

### **7.3.19 Entrenched Rights**

Entrenched Rights are rights that cannot be modified or waived in accordance with the STID without the consent of the Secured Creditor having the Entrenched Right.

The Entrenched Rights of the Class A Debt Providers include, subject to certain provisions of the CTA including the right to amend financial ratios following a Periodic Review or as a result of a material change in the regulation of the water industry in the United Kingdom, any proposed modification to, or consent or waiver under or in respect of the STID or any other Finance Document which:

- (i) the relevant Class A Debt Provider (or, where applicable, its Secured Creditor Representative) has demonstrated to the satisfaction of the Security Trustee would increase or adversely modify its obligations or liabilities thereunder or in connection therewith;
- (ii) (a) would release of any of the Security (unless equivalent replacement security is taken at the same time) unless such release is permitted in accordance with the terms of the STID and the relevant Security Document or (b) would alter the rights of priority of or the enforcement by the relevant Class A Debt Provider (or, where applicable, its Secured Creditor Representative) under the Security Documents other than as expressly contemplated therein;
- (iii) would change or would relate to the Payment Priorities;
- (iv) would change or would relate to the Entrenched Rights or the Reserved Matters or, where applicable, the relevant Class A Debt Provider’s Entrenched Rights or Reserved Matters;
- (v) would change or would relate to (a) the definitions of “Class A DIG”, “Class A DIG Representatives”, “DIG Proposal”, “DIG Directions Request”, “Majority Creditors”,

“Qualifying Class A Debt” or “Voted Qualifying Class A Debt”, (b) those matters expressly requiring the consent, approval or agreement of, or directions or instructions from, or waiver by the Majority Creditors or the Security Trustee or (c) the percentages of Outstanding Principal Amount of Qualifying Class A Debt required to terminate a Standstill;

- (vi) would delay the date fixed for payment of principal, interest or Make-Whole Amount in respect of the relevant Class A Debt Provider’s Class A Debt or of any fees or premia in respect thereof or would reduce the amount of principal, interest or Make-Whole Amount payable in respect of such Class A Debt or the amount of any fees or premia in respect thereof;
- (vii) would bring forward the date fixed for payment of principal, interest or Make-Whole Amount in respect of Class A Debt or Class B Debt or any fees or premia in respect thereof or would increase the amount of principal, interest or Make-Whole Amount payable on any date in respect of Class A Debt or Class B Debt or any fees or premia in respect thereof;
- (viii) would result in the exchange of the relevant Class A Debt Provider’s Class A Debt for, or the conversion of such Class A Debt into, shares, bonds or other obligations of any other person;
- (ix) would change or would relate to the currency of payment due under the relevant Class A Debt Provider’s Class A Debt (other than due to the United Kingdom joining the euro);
- (x) would change Anglian Water’s information and reporting covenants or (in respect of the USPP Bondholders only) the additional information and reporting covenants and covenants relating to inspection rights contained in the documents relating to the USPP Bonds in issue on the Effective Date;
- (xi) would change the change of control undertakings;
- (xii) would change or would relate to Anglian Water’s negative pledge, financial indebtedness and restricted payments covenants;
- (xiii) would change or would relate to, but not waive (subject to (xiv) below), the Trigger Events, Trigger Event Consequences, Trigger Event Remedies or Events of Default;
- (xiv) would result in a waiver of the credit downgrade Trigger Event (see 7.5.7(ii), “*Trigger Events – Credit Rating Downgrade*”), a non-payment Event of Default in respect of any Obligor, Events of Default relating to financial ratios and credit rating downgrades (see 7.5.10(i), (xix) and (xx), “*Events of Default*” including their effect as a Trigger Event);
- (xv) would change or would relate to the rights of the relevant Class A Debt Provider to receive any sums owing to it for its own account in respect of premia, fees, costs, charges, liabilities, damages, proceedings, claims and demands in relation to any Finance Document to which it is a party (excluding, for the avoidance of doubt, the principal, interest or Make-Whole Amount payable to the relevant Class A Debt Provider);
- (xvi) would change or would relate to any existing obligation of an Obligor to gross up any payment in respect of the relevant Class A Debt Provider’s Class A Debt in the event of the imposition of withholding taxes;
- (xvii) would relate to a substitution of the Issuer in circumstances where the relevant USPP Bondholder has demonstrated to the satisfaction of the Security Trustee that such substitution would adversely affect the tax treatment of their holding of USPP Bonds; or
- (xviii) would have the effect of changing certain notice, reporting and solicitation provisions relating to the USPP Bonds.

The Entrenched Rights of the Class B Debt Providers include, subject to certain provisions of the CTA including the right to amend financial ratios following a Periodic Review or as a result of a material change in the regulation of the water industry in the United Kingdom, any proposed

modification to, or consent or waiver under or in respect of, the STID or any other Finance Document which:

- (i) the relevant Class B Debt Provider (or, where applicable, its Secured Creditor Representative) has demonstrated to the satisfaction of the Security Trustee would increase or adversely modify its obligations or liabilities thereunder or in connection therewith;
- (ii) (a) would release any of the Security (unless equivalent replacement security is taken at the same time) unless such release is permitted in accordance with the terms of the STID and the relevant Security Document or (b) would alter the rights of priority of or the enforcement by the relevant Class B Debt Provider (or, where applicable, its Secured Creditor Representative) under the Security Documents other than as expressly contemplated therein;
- (iii) would change or would relate to the Payment Priorities;
- (iv) would change or would relate to the Entrenched Rights or the Reserved Matters or, where applicable, the relevant Class B Debt Provider's Entrenched Rights or Reserved Matters;
- (v) would change or would relate to (a) the definitions of "Class B DIG", "Class B DIG Representatives", "DIG Proposal", "DIG Directions Request", "Majority Creditors", "Qualifying Class B Debt" or "Voted Qualifying Class B Debt", (b) those matters expressly requiring the consent, approval or agreement of, or directions or instructions from, or waiver by the Majority Creditors or the Security Trustee or (c) the percentages of Outstanding Principal Amount of Qualifying Class B Debt required to terminate a Standstill;
- (vi) would delay the date fixed for payment of principal, interest or Make-Whole Amount in respect of the relevant Class B Debt Provider's Class B Debt or any fees or premia in respect thereof or would reduce the amount of principal, interest or Make-Whole Amount payable on any date in respect of such Class B Debt or any fees or premia in respect thereof;
- (vii) would bring forward the date fixed for payment of principal, interest or Make-Whole Amount in respect of Class A Debt or Class B Debt or any fees or premia in respect thereof or would increase the amount of principal, interest or Make-Whole Amount payable on any date in respect of Class A Debt or Class B Debt or any fees or premia in respect thereof;
- (viii) would result in the exchange of the relevant Class B Debt Provider's Class B Debt for, or the conversion of such Class B Debt into, shares, bonds or other obligations of any other person;
- (ix) would change or would relate to the currency of payment under the relevant Class B Debt Provider's Class B Debt (other than due to the United Kingdom joining the euro);
- (x) would change Anglian Water's information and reporting covenants;
- (xi) would change the change of control undertakings;
- (xii) would change or would relate to Anglian Water's negative pledge, financial indebtedness and restricted payments covenants;
- (xiii) would change or would relate to, but not waive (subject to (xiv) below), the Trigger Events, Trigger Event Consequences, Trigger Event Remedies or Events of Default;
- (xiv) would result in a waiver of the credit downgrade Trigger Event (see 7.5.7(ii), "*Trigger Events – Credit Rating Downgrade*"), a non-payment Event of Default in respect of any Obligor, Events of Default relating to financial ratios and credit rating downgrades (see 7.5.10(i), (xix) and (xx), "*Events of Default*" including their effect as a Trigger Event);
- (xv) would change or would relate to the rights of the relevant Class B Debt Provider to receive any sums owing to it for its own account in respect of premia, fees, costs, charges,

liabilities, damages, proceedings, claims and demands in relation to any Finance Document to which it is a party (excluding, for the avoidance of doubt, the principal, interest or Make-Whole Amount payable to the relevant Class B Debt Provider); and

- (xvi) would change or would relate to any existing obligation of an Obligor to gross up any payment in respect of the relevant Class B Debt Provider's Class B Debt in the event of the imposition of withholding taxes.

The Entrenched Rights of the Finance Lessors include, in addition to the Entrenched Rights of the Class A Debt Providers set out above, any proposed modification to, or consent or waiver under or in respect of the STID or any other Finance Document which would change or relate to:

- (i) any sale, transfer or other disposal (whether deemed or otherwise) of any of the Equipment;
- (ii) the affixing of any Equipment to any land or building to which Anglian Water or the Issuer (as applicable) does not have an interest in such land for the purposes of the Capital Allowances Act 2001;
- (iii) the creation or subsistence of any encumbrance, lien, mortgage or other Security Interest over any Equipment;
- (iv) any of the covenants or representations and warranties set out in the Finance Documents which relate to the maintenance or condition of the Equipment;
- (v) any provision(s) contained in the Finance Documents pertaining to any damage, destruction or total loss of any of the Equipment;
- (vi) any elections filed with the United Kingdom Inland Revenue by Anglian Water or the Issuer (as applicable) and any Finance Lessor under the Finance Leases pursuant to Sections 177 and/or 227 of the Capital Allowances Act 2001 in respect of the Equipment and the relevant Finance Lessor's expenditure on the Equipment;
- (vii) the obligations of Anglian Water or the Issuer (as applicable) to reserve amounts monthly, as set out in the cash management arrangements, that reduces the amount which it is required to reserve;
- (viii) the provisions relating to the calculation of rental payments and/or sums due upon termination of the leasing of any Equipment; and
- (ix) any changes to the Entrenched Rights of the Finance Lessors set out in paragraph (i) to (viii) above.

The Entrenched Rights of the Class A Debt Providers, the Class B Debt Providers and the Finance Lessors (where applicable) will be exercised through their Secured Creditor Representatives.

The Bond Trustee, the Security Trustee and the Financial Guarantor have certain other limited Entrenched Rights in relation to any provisions of the Finance Documents that generally affect them to a greater extent than others.

### **7.3.20 Reserved Matters**

Reserved Matters are matters which, subject to the Intercreditor Arrangements and the CTA, a Secured Creditor is free to exercise in accordance with its own facility arrangements and so are not exercisable by or by direction of the Majority Creditors.

Those Reserved Matters which the Secured Creditors reserve to themselves to decide are each and every right, power, authority and discretion of, or exercisable by, the Secured Creditors at any time:

- (i) to receive any sums owing to it for its own account in respect of premia, fees, costs, charges, liabilities, damages, proceedings, claims and demands in relation to any Finance Document to which it is a party (as permitted under the CTA);

- (ii) to make determinations of and require the making of payments due and payable to it under the provisions of the Finance Documents (as permitted under the CTA);
- (iii) to exercise the rights vested in it or permitted to be exercised by it under and pursuant to the CTA and the STID;
- (iv) to receive notices, certificates, communications or other documents or information under the Finance Documents or otherwise;
- (v) in the case of each Finance Lessor, to inspect the relevant Equipment, to make calculations under the financial schedules to the relevant Finance Lease (or the equivalent provisions thereunder relating to the calculation of Rental or termination sums) and to terminate the relevant Finance Lease provided such termination is a Permitted Lease Termination;
- (vi) in the case of each Hedge Counterparty, to terminate the relevant Hedging Agreement provided such termination is a Permitted Hedge Termination;
- (vii) in the case of the Original Lenders to accelerate the Class B Debt portion of the Bridging Facility provided such acceleration is a Permitted Acceleration (as set out in the STID); and
- (viii) in the case of any Secured Creditor to accelerate their claims, to the extent necessary to apply proceeds of enforcement of the share pledges provided by Anglian Water Services Holdings Ltd and Anglian Water Services Overseas Holdings Ltd pursuant to the terms of the Security Documents.

The Bond Trustee, the Security Trustee and the Financial Guarantor each have certain additional Reserved Matters which each has reserved to itself to decide. For the Bond Trustee and the Financial Guarantor, these include rights vested in it pursuant to the terms of the Bond Trust Deed and the Bond Policy and for the Security Trustee, these include rights vested in it pursuant to the terms of the STID.

Those Reserved Matters which the Bond Trustee reserves to itself are every right, power, authority and discretion of, or exercisable by, the Bond Trustee (in respect of paragraphs (o) to (u) below, in relation to any Series of Class A Unwrapped Bonds (other than USPP 2001 Bonds) or Class B Unwrapped Bonds and (where an FG Event of Default has occurred and is continuing) Class A Wrapped Bonds or Class B Wrapped Bonds), whether expressed as a right, power, authority or discretion of the Bond Trustee or obligation of any other party:

- (a) to make any determination contemplated or required under the Bond Trust Deed or the relevant Existing Bond Trust Deed as to the occurrence or otherwise of an FG Event of Default, in relation to its Reserved Matters and in relation to its Entrenched Rights;
- (b) to agree to make any amendment or any waiver or consent which has the effect of resulting in or permitting any amendment to the provisions of any Bond Policy;
- (c) to make any claim under, or enforce any provision of, any Bond Policy;
- (d) which is provided for the purpose of enabling the Bond Trustee to protect its own position and interests in its personal capacity (including its own personal financial interests) or which the Bond Trustee determines to be necessary or appropriate to exercise for the protection of its own position and interests in its personal capacity;
- (e) to determine amounts due in relation to and to claim under indemnities in favour of the Bond Trustee in its own capacity or for and on behalf of Bondholders under the Finance Documents;
- (f) to receive any amounts owing to it for its own account in accordance with the provisions of the Finance Documents;
- (g) to determine the amount of sums due in relation to expenses and stamp duties pursuant to the Finance Documents;

- (h) to make a claim for expenses under the Finance Documents;
- (i) to receive notices, certificates, communications or other documents or information under the Finance Documents or otherwise;
- (j) which relieves or exempts the Bond Trustee from liability and exculpates or exonerates it (including, without limitation, any right of the Bond Trustee under any of the Finance Documents to make assumptions as to, or rely on any notice, certificate or other communication confirming, the existence or non-existence of any act, circumstance or event);
- (k) against or in relation to the relevant Bondholders;
- (l) to agree any amendment to Part 2 (Bond Trustee Reserved Matters) of Schedule 3 of the STID;
- (m) under the Third Schedule (Provisions for Meetings of Bondholders) of the Bond Trust Deed or the equivalent schedule of the relevant Existing Bond Trust Deed;
- (n) the right to appoint a co-trustee or to retire under, as the case may be, Clause 23 (New Bond Trustee) and Clause 24 (Bond Trustee's Retirement and Removal) of the Bond Trust Deed or the equivalent clauses of the relevant Existing Bond Trust Deed;
- (o) the publication of an Interest Rate or Interest Amount, as the case may be, in accordance with Condition 7(b)(iv) or the equivalent condition of the relevant Existing Bonds;
- (p) the determination of amounts, as the case may be, in accordance with Condition 7(b)(vi) or the equivalent condition of the relevant Existing Bonds;
- (q) the selection of an Indexation Adviser, as the case may be, in accordance with Condition 9(c)(ii)A or the equivalent condition of the relevant Existing Bonds;
- (r) the consideration and approval in relation to a substitute index figure, as the case may be, in accordance with Condition 9(c)(ii) or the equivalent condition of the relevant Existing Bonds;
- (s) the approval in relation to the Issuer being required to deduct or withhold amounts, as the case may be, in accordance with Condition 11;
- (t) the variation, termination and appointment of Agents, as the case may be, in accordance with Condition 16 or the equivalent condition of the relevant Existing Bonds; and
- (u) to consent to any proposed amendment to, as the case may be, the Bond Trust Deed or the relevant Existing Bond Trust Deed, the relevant Conditions or any Finance Document to which it is a party whether such consent is sought to correct a manifest error or is of a formal, minor or technical nature (and, for the avoidance of doubt, any other matter referred to in Clause 19 (Waiver, Authorisation and Determination) of the Bond Trust Deed or the equivalent Clause of the relevant Existing Bond Trust Deed involving the decision of the Bond Trustee to waive or modify any provisions of the documents referred to therein will be subject to the directions of the Majority Creditors).

Those Reserved Matters which the Financial Guarantor reserves to itself are each and every right, power, authority and discretion of, or exercisable by, the relevant Financial Guarantor at any time in respect of the Class A Wrapped Bonds or Class B Wrapped Bonds for which it has issued a Bond Policy (prior to an FG Event of Default which is continuing) in relation to:

- (a) the publication of an Interest Rate or Interest Amount in accordance with Condition 7(b)(iv) or the equivalent condition of the relevant Existing Bonds;
- (b) the determination of amounts in accordance with Condition 7(b)(vi) or the equivalent condition of the relevant Existing Bonds;



- (c) the selection of an Indexation Adviser in accordance with Condition 9(c)(ii)A or the equivalent condition of the relevant Existing Bonds;
- (d) the consideration and approval in relation to a substitute index figure in accordance with Condition 9(c)(ii) or the equivalent condition of the relevant Existing Bonds;
- (e) the approval in relation to the Issuer being required to deduct or withhold amounts in accordance with Condition 11;
- (f) the variation, termination and appointment of Agents in accordance with Condition 16 or the equivalent condition of the relevant Existing Bonds; and
- (g) any amendment to Part 3 (Financial Guarantor Reserved Matters) of Schedule 3 of the STID.

Those Reserved Matters which the Security Trustee reserves to itself are each and every right, power, authority and discretion of, or exercisable by, the Security Trustee, whether expressed as a right, power, authority or discretion of the Security Trustee or an obligation of any other party:

- (a) pursuant to the STID;
- (b) to receive any sums owing to it for its own account in respect of fees, costs, charges, liabilities, damages, proceedings, claims and demands in performing its powers and exercising its discretions under the STID and any other Finance Document to which the Security Trustee is a party;
- (c) which is provided for the purpose of enabling the Security Trustee to protect its own position and interests in its personal capacity (including its own personal financial interest) or which the Security Trustee determines to be necessary or appropriate to exercise for the protection of its own position and interests in its personal capacity;
- (d) except as otherwise specifically provided herein to apply any of the sums referred to in Clause 15 (Activities of the Security Trustee) of the STID in accordance with such Clause;
- (e) to receive notices, certificates, communications or other documents or information, to direct that such notices, certificates, communications or other documents or information must be provided (or must not be provided) to it or any other party, or, where applicable, to determine the form and content of any notice, certificate, communication or other document;
- (f) which relieves or exempts the Security Trustee from liability or exculpates or exonerates it (including, without limitation, any right of the Security Trustee under any of the Finance Documents to make assumptions as to, or rely on any notice, certificate or other communication confirming, the existence or non-existence of any act, circumstance or event);
- (g) to agree to any amendment to Part 1 (Security Trustee Reserved Matters) of Schedule 3 of the STID;
- (h) to determine amounts due in relation to and to claim under indemnities in favour of the Security Trustee under Clause 15.5 (Indemnification of the Security Trustee) or Clause 16 (Remuneration and Indemnification of the Security Trustee) of the STID or pursuant to any other Finance Documents;
- (i) to appoint a co-trustee or to retire under Clause 17 (Appointment of Additional Trustees) and Clause 19.6 (Resignation of the Security Trustee) of the STID; and
- (j) to agree modifications to, or give any consent or grant any waiver under or in respect of, any term of the STID or any other Finance Document to which the Security Trustee is a party or over which it has Security under the Security Documents in accordance with Clause 8.1 (Procedures for Modifications, Consents and Waivers) of the STID.

### 7.3.21 Substitution of the Issuer

The Security Trustee shall implement any STID Proposal proposing the substitution in place of the Issuer, or any substituted Issuer, as the principal debtor under the Finance Documents of any other company incorporated in any other jurisdiction meeting the criteria for such a single purpose company established from time to time by the Rating Agencies.

## 7.4 Intercompany Loan Arrangements

Under the terms of the licence modifications, Anglian Water is prohibited from entering into loans with its associates without the consent of the Director General. The Director General has confirmed that he will not treat the following as being in breach of those conditions.

### 7.4.1 Anglian Water Loan Notes

Anglian Water issued loan notes to the Issuer on the Effective Date in an aggregate amount equal to the Sterling equivalent of the aggregate Outstanding Principal Amount of the Existing Bonds and the Transferred USPP Bonds other than the £100,000,000 51/8 per cent. index-linked loan stock due 2008 and the £150,000,000 3.875 per cent. index-linked guaranteed notes due 2020, in each case of AWG Group Ltd (the “**Existing Index-Linked Bonds**”). In addition, Anglian Water procured the assignment to the Issuer and subsequent amendment of AWG Group Ltd’s rights under the existing intercompany loans from AWG Group Ltd to Anglian Water relating to such Existing Index-Linked Bonds. The issue of the loan notes and the assignment and amendment of such intercompany loans comprised the consideration for the assumption by the Issuer of the primary obligations under the Existing Bonds, the Transferred USPP Bonds and the related Hedging Agreements. References to such loan notes issued by Anglian Water and the rights of the Issuer under such assigned intercompany loans are hereinafter referred to as the “**Anglian Water Loan Notes**”.

Each series of bonds comprising the Existing Bonds and Transferred USPP Bonds is represented by a separate Anglian Water Loan Note. The interest rate in respect of each such Anglian Water Loan Note is equivalent to the rate of interest on the corresponding series of bonds, or if hedged, at the hedged rate. Similarly, each Anglian Water Loan Note will be redeemed (in whole or in part) immediately prior to the date upon which any payment of principal is to be made on the corresponding series of bonds. The Issuer charges Anglian Water an annual management fee in respect of holding the Anglian Water Loan Notes.

### 7.4.2 Issuer/Anglian Water Loan Agreement

The Issuer has on-lent and will on-lend an amount equal to the Sterling equivalent of the gross proceeds of issue of each Series of Bonds and each drawing or other obligation for Financial Indebtedness under each Authorised Credit Facility (as adjusted by any applicable Hedging Agreements) entered into on or after the Effective Date to Anglian Water under the terms of a loan agreement (the “**Issuer/Anglian Water Loan Agreement**” and, together with the Anglian Water Loan Notes, the “**Intercompany Loan Arrangements**”). All advances to be made by the Issuer under the Issuer/Anglian Water Loan Agreement have been in Sterling and at rates of interest set out in the relevant Final Terms or, if hedged in accordance with the Hedging Policy (see 7.10, “*Hedging Agreements*” below) at the hedged rate. The repayment of each advance corresponding to a Bond issue shall be on the repayment terms of such Bonds. The Issuer charges Anglian Water an annual management fee in respect of entering into the Issuer/Anglian Water Loan Agreement.

### 7.4.3 Initial Advance and further Advances

The first advance under the Issuer/Anglian Water Loan Agreement comprised an amount equal to the Sterling equivalent of the gross proceeds of the issue of Bonds under the Programme, the gross proceeds of drawings under Tranche A of the Bridging Facility and drawings under the Initial Authorised Loan Facility on the Effective Date, after having exchanged the proceeds of each Series of Bonds denominated in a currency other than Sterling pursuant to the initial currency exchange under the Currency Hedging Agreements with the Existing Hedge Counterparties in respect of such Series of Bonds.

Further advances under the Issuer/Anglian Water Loan Agreement will, *inter alia*, comprise of amounts equal to the Sterling equivalent of the gross proceeds of the issue of Bonds under the

Programme. It is the relevant advance under the Issuer/Anglian Water Loan Agreement which is the asset backing the corresponding relevant issue of Bonds. Advances under the Issuer/Anglian Water Loan Agreement along with the Transaction Documents have the characteristics that demonstrate capacity to produce funds to service any payments due and payable on the Bonds.

#### **7.4.4 Fees Generally**

Under the terms of the Intercompany Loan Arrangements, Anglian Water is required to pay fees to the Issuer in an amount equal to all premia, fees, costs, charges and other expenses payable by the Issuer in connection with financial accommodation provided to Anglian Water.

#### **7.4.5 UK Holdco/Anglian Water Loan**

On the Effective Date, Anglian Water entered into the UK Holdco/Anglian Water Loan with Anglian Water Services Holdings Ltd. This enabled Anglian Water Services Holdings Ltd to satisfy obligations to pay to AWG Group Ltd the consideration for the acquisition of shares in Anglian Water Services Overseas Holdings Ltd. The UK Holdco/Anglian Water Loan bears interest at a commercial rate. Interest under the UK Holdco/Anglian Water Loan is payable subject to restrictions. See 7.5.5(iv)(v)(E), “*Covenants – General*” below.

#### **7.4.6 Subordinated Liabilities**

All present and future liabilities payable or owing by one member of the Anglian Water Services Financing Group to another member of the Anglian Water Services Financing Group comprise subordinated liabilities other than liabilities under the Intercompany Loan Arrangements.

### **7.5 Common Terms Agreement**

#### **7.5.1 General**

Each of the Finance Lessors, the Hedge Counterparties, the Security Trustee, the Cash Manager, the Original Lenders, the Liquidity Facility Providers, the Authorised Credit Providers, each Obligor, the Bond Trustee, the Initial Financial Guarantor, the Registrar, the Principal Paying Agent, the Transfer Agent, the Exchange Agent, and the USPP 2001 Bondholders and others entered into a common terms agreement (the “**Common Terms Agreement**” or “**CTA**”). The Common Terms Agreement sets out the representations, covenants (positive, negative and financial), Trigger Events and Events of Default which apply to each Authorised Credit Facility (including for the avoidance of doubt the Intercompany Loan Arrangements, Finance Leases, Hedging Agreements and any other document entered into in connection with an Authorised Credit Facility).

It is a term of the Common Terms Agreement that any representations, covenants (to the extent of being able to declare an Event of Default), Trigger Events and Events of Default contained in any document which is in addition to those in the Common Terms Agreement are (save for limited exceptions which, *inter alia*, include covenants relating to indemnities, covenants to pay, remuneration, costs and expenses, covenants in each Series of Bonds issued on the Effective Date, those contained in the Programme Agreement, the Bond Trust Deed, the Indemnification Deed, the Tax Deed of Covenant and the Agency Agreement to the extent such apply to any Series of Bonds, certain provisions under the Hedging Agreements, the Finance Leases and the mandatory prepayment rights and obligations under the Bridging Facility) unenforceable. The Common Terms Agreement allows Anglian Water (following a Periodic Review or any material change in the regulation of the water industry in the United Kingdom) to amend any financial ratio contained within the covenants, Trigger Events or Events of Default, provided that each Financial Guarantor and the Security Trustee (acting on the instructions of the Majority Creditors) agree and the Rating Requirement has been met.

The Common Terms Agreement also sets out the cash management arrangements to apply to Anglian Water Services Financing Group (see 7.6, “**Cash Management**” below). It is a requirement of the Common Terms Agreement that future providers of Class A Debt and Class B Debt must also accede to the Common Terms Agreement and the STID.

A summary of the representations, covenants, Trigger Events and Events of Default included in the Common Terms Agreement is set out below.

## 7.5.2 Representations

On the Effective Date each Obligor made, (and in respect of certain representations on each Issue Date, each Payment Date, on the date of the Initial Bond Policy, on the day any new Authorised Credit Facility or any new Tier 1 Material Agreement is entered into and only in relation to such agreements, and on each date for payment of a Restricted Payment into the Distributions Account or Customer Payments Account or for a payment of a UK Holdco Debt Service Distribution each Obligor will make), a number of representations in respect of itself to each Finance Party. These representations did and will (amongst others) include (subject, in some cases, to agreed exceptions and qualifications as to materiality and reservations of law) representations as to:

- (i) its corporate status, power and authority (a) to enter into and perform its obligations under the Transaction Documents and (b) to own, lease and operate its assets and to carry on its business;
- (ii) its obligations under the Transaction Documents being its legal, valid and enforceable obligations;
- (iii) its entry into and performance under the Transaction Documents not conflicting with any document which is binding upon its assets, its constitutional documents or any material applicable law;
- (iv) the preparation of its financial statements in accordance with Applicable Accounting Principles;
- (v) the validity and admissibility in evidence of the Finance Documents in any proceedings in the jurisdiction of its incorporation;
- (vi) the Security Documents to which it is party conferring the Security Interests they purport to confer and such Security Interests not being subject to any prior or *pari passu* Security Interest (other than Permitted Security Interest);
- (vii) the conduct of its business not violating any judgment, law or regulation, which if enforced would have a Material Adverse Effect;
- (viii) no Default or Potential Trigger Event being outstanding;
- (ix) the obtaining by it prior to the Effective Date of all consents and approvals necessary for the conduct of Anglian Water's business and the transactions in the Finance Documents;
- (x) its ownership of, or interests in, the assets over which it has created Security Interests under the Security Documents and which are material to the operation of its business;
- (xi) insurances required to be maintained under any Finance Document being in full force and effect;
- (xii) there being no insolvency event in relation to it;
- (xiii) the ownership structure of the Anglian Water Services Financing Group;
- (xiv) the due payment of all its taxes (save to the extent any tax payment is being disputed in good faith);
- (xv) under the laws of its jurisdiction of incorporation and tax residence in force on the Effective Date, it not (other than as disclosed) being required to make any deduction or withholding from any payment of interest in circumstances where, under current United Kingdom law, no United Kingdom withholding tax would be imposed on the payment;
- (xvi) subject to certain reservations as to matters of law, the choice of English law being recognised and enforced in proceedings against Anglian Water Services Overseas Holdings Ltd;
- (xvii) the claims of Secured Creditors ranking prior to the claims of its other unsecured and unsubordinated creditors;

- (xviii) no Security Interest having been created, or allowed to exist, other than Permitted Security Interests and no indebtedness incurred other than Permitted Financial Indebtedness or any Permitted Volume Trading Arrangements;
- (xix) the Bonds constituting (or constituting upon execution, due authentication and delivery) legal and valid obligations binding on the Issuer and enforceable against it in accordance with its terms and constituting evidence of direct, secured and unconditional obligations of the Issuer;
- (xx) no litigation or other proceedings current, or to its knowledge pending or threatened against it or its assets;
- (xxi) limits on its powers not being exceeded as a result of the borrowing, leasing, granting of security or giving or guarantees contemplated by the Transaction Documents;
- (xxii) compliance with environmental laws and having obtained all environmental permits necessary for conduct of its business and no environmental claim having been commenced;
- (xxiii) loans not having been made to other persons other than pursuant to Finance Documents, the UK Holdco/Anglian Water Loan, Permitted Volume Trading Arrangements and the Intercompany Loan Arrangements;
- (xxiv) Treasury Transactions not having been entered into other than the Hedging Agreements;
- (xxv) all arrangements or contracts with any person (including Affiliates) being on arm's length basis and on terms no less favourable to it than would reasonably be expected to be obtained in a comparable arm's length transaction with a person not being an Affiliate, unless permitted under the Finance Documents, as a result of a Permitted Emergency Action, certain disclosed transactions up to the next Periodic Review or save as disclosed in this Prospectus; and
- (xxvi) on the Effective Date, no member of the Anglian Water Services Financing Group being liable in any manner in respect of any Financial Indebtedness (including by way of primary obligor, guarantor, surety or any other manner) that is not either Class A Debt or Class B Debt, the providers of which have executed the CTA and the STID, or Permitted Financial Indebtedness falling within the category listed in paragraphs (a), (b), (d) or (e) of the definition of Permitted Financial Indebtedness.

Additionally, Anglian Water (subject, in some cases, to agreed exceptions and qualifications as to materiality and reservations of law) represented:

- (i) to the best of its knowledge, it has the right to use intellectual property rights necessary to conduct its Business;
- (ii) to the best of its knowledge (and save as disclosed to the Security Trustee) all parties to Transaction Documents are in compliance with the Transaction Documents;
- (iii) assumptions used in respect of financial ratio calculations having been made in good faith, after due and careful consideration and being consistent with Applicable Accounting Principles and Good Industry Practice;
- (iv) it is not aware of any Special Administration Order having been made in respect of it; and
- (v) the accuracy (in all material respects) of certain written information provided by Anglian Water and the accuracy of this Prospectus.

The representation referred to in sub-paragraph (ii) was made by Anglian Water on the date of the Common Terms Agreement and has been made and will be made on the date of each Investors Report, directors certificate, compliance certificate or interim compliance certificate. The representation referred to in sub-paragraph (iv) was made by Anglian Water on the date of the Common Terms Agreement, and, subject to minor amendments, on each date when any new Authorised Credit Facility has been or is entered into when it is generally syndicated.

Additionally, the other members of the Anglian Water Services Financing Group represented that they have not carried on any business since the date of their incorporation other than that required in connection with their formation and capitalisation and/or as envisaged by the Transaction Documents.

### **7.5.3 Covenants**

The Common Terms Agreement contains certain covenants from each of the Obligors. A summary of the covenants which are (amongst others) included (subject, in some cases, as to agreed exceptions, *de minimis* amounts and qualifications as to materiality and reservations of law) in the Common Terms Agreement is set out below in 7.5.4, “*Information – Covenants*”, 7.5.5, “*Covenants – General*” and 7.5.6, “*Financial Covenants*”.

### **7.5.4 Information – Covenants**

- (i) So far as permitted by any applicable law or any binding confidentiality obligation, Anglian Water has undertaken to supply to the Security Trustee certain information such as:
  - (a) a copy of all information, which would reasonably be expected to be material to an Authorised Credit Provider to the Anglian Water Services Financing Group, which it supplies to the Director General;
  - (b) as soon as reasonably practicable after becoming aware, details of any proposed material changes to the Instrument of Appointment or any proposed changes to the constitutional documents of any member of the Anglian Water Services Financing Group;
  - (c) promptly upon becoming aware, details of any actual or potential enquiry, investigation or proceeding commenced by any government, court, regulatory agency or authority, if such enquiry, investigation or proceeding would be reasonably likely to have a Material Adverse Effect;
  - (d) as soon as reasonably practicable after receipt, any material notice (including an enforcement notice) from any governmental authority or industry regulator (including Ofwat) received by Anglian Water;
  - (e) copies of all certificates and responses provided by Anglian Water or any member of the Anglian Water Services Financing Group to any industry regulator (including Ofwat) which would reasonably be expected to be material and adverse and which relates to the creditworthiness of Anglian Water or Anglian Water’s ability to perform its duties under the Instrument of Appointment;
  - (f) copies of all reports and information provided by the operator and/or service provider to it under any Material Agreement which would be material or adverse in relation to the creditworthiness of Anglian Water or to Anglian Water’s ability to perform its duties under the Instrument of Appointment, and Anglian Water shall use reasonable endeavours to procure that any such Material Agreements permit such reports and information to be disclosed to the Secured Creditors;
  - (g) a semi-annual Investors Report;
  - (h) such material information about the business and financial condition of Anglian Water as a Secured Creditor may reasonably and properly request, from time to time, on the request of the Security Trustee (as directed by such Secured Creditor); and
  - (i) details of any Bondholder accepting the offer of prepayment following the occurrence of an Early Redemption Event and the aggregate Early Redemption Amount payable.
- (ii) Anglian Water has further agreed to provide information regarding a UK Holdco Change of Control to the Security Trustee and the Financial Guarantor as soon as it becomes aware

of any such proposal and to use all reasonable endeavours to procure that the Security Trustee and such Financial Guarantor have been given a reasonable opportunity to express views on the identity and role of any such proposed new Controlling person under a UK Holdco Change of Control.

- (iii) Anglian Water has further agreed to use all reasonable endeavours to supply any information due to, or requested by, the Director General within the time period provided for supply of such information. If no time period is specified, Anglian Water must provide the required information as soon as reasonably practicable. This is subject to action Anglian Water reasonably believes is consistent with prudent management as part of negotiation with the Director General.
- (iv) Additionally, each Obligor has undertaken to supply to the Security Trustee:
  - (a) its audited financial statements and, in the case of Anglian Water, its audited consolidated financial statements, for each of its financial years and, in the case of Anglian Water, its unaudited consolidated financial interim statements, for the first half-year of each of its financial years;
  - (b) copies of all material documents despatched by it to its shareholders or creditors generally; and
  - (c) as soon as reasonably practicable after becoming aware or available, details of:
    - (A) any litigation or other proceedings (which alone or in aggregate could reasonably be expected to give rise to a claim against Anglian Water of £5,000,000 (indexed)), which are current, threatened or pending and would be reasonably likely, if adversely determined, to have a Material Adverse Effect;
    - (B) the periodic information relating to it (such as Anglian Water's annual charges scheme, a summary of Anglian Water's strategic business plan at each Periodic Review, Anglian Water's procurement plans, Anglian Water's annual drinking water quality report, Anglian Water's annual environmental report and Anglian Water's annual conservation and access report);
    - (C) any event which could reasonably be expected to give rise to an insurance claim in excess of £4,000,000 (indexed);
    - (D) any Material Entity Event (see 7.5.11, "*Material Entity Events*" below) and/or Emergency which would be reasonably likely to have a Material Adverse Effect;
    - (E) any non-compliance with any law or regulation which would be reasonably likely to have a Material Adverse Effect;
    - (F) any other event which would be reasonably likely to have a Material Adverse Effect; and
  - (d) such material information as is reasonably and properly requested by any Secured Creditor; and
  - (e) notification of any Default or Potential Trigger Event relating to it promptly upon becoming aware of its occurrence (and the steps, if any, being taken to remedy it).
- (v) Additionally, each of Anglian Water and the Issuer has undertaken *inter alia*:
  - (a) to supply a compliance certificate signed by two authorised signatories of the Issuer and two independent non-executive directors of Anglian Water (subject to any vacancies arising out of exceptional circumstances not in the normal course of business, in which case, the signature of only one independent non-executive director of Anglian Water will be required); such compliance certificate to be

accompanied by a statement as to what the historical financial ratios which are required to be calculated under the Common Terms Agreement are, a short summary of the manner in which the historical financial ratios have been calculated and a certification of compliance in relation to projected financial ratios;

- (b) to permit the Security Trustee to investigate the calculations contained in any accompanying statement to a compliance certificate and to call for other substantiating evidence if it certifies to Anglian Water or the Issuer that it has reason to believe that the historical ratios set out in the statement are incorrect or misleading or in the event that there is a deterioration in the historical ratios and will have the right to call for further information if it considers that Anglian Water can have no reasonable grounds for confirming that it is in compliance with all forward looking ratios; and
  - (c) to deliver to the Security Trustee promptly after any reasonable request made by the Security Trustee, a certificate signed on its behalf by two of its authorised signatories (a) certifying that no Default or Potential Trigger Event is outstanding of which it is aware, having made all reasonable enquiries, or if it is outstanding, specifying the Default or Potential Trigger Event and the steps (if any) taken or proposed to be taken to remedy such event.
- (vi) In addition, each Obligor in respect of information delivered electronically:
- (a) may deliver any information under the Common Terms Agreement to a Secured Creditor by posting it on an electronic website, provided the Obligor and the Security Trustee have designated a website and the Obligor has notified the Security Trustee and each relevant Secured Creditor of the address and password for such website; and
  - (b) must notify the Security Trustee if (i) the website cannot be accessed or the website or any information on it is infected for a period of 5 consecutive days, in which case the Obligor must supply the Security Trustee with all information required under the Common Terms Agreement in paper form with copies as requested by any Finance Party or (ii) if the password is changed.

#### **7.5.5 Covenants – General**

- (i) Each Obligor has undertaken *inter alia*:
  - (a) to do all such things as are necessary to maintain its corporate status where failure would be reasonably likely to have a Material Adverse Effect or otherwise adversely affect the Security Interests of the Secured Creditors;
  - (b) to comply with its cash management obligations (if any) set out in the Common Terms Agreement;
  - (c) to ensure that the claims of Secured Creditors against it under the Finance Documents will rank (subject to certain reservations as to matters of law) prior to or at least *pari passu* with the claims of all its other unsecured and unsubordinated creditors save for those whose claims are preferred solely by law;
  - (d) to operate and maintain, or ensure the operation and maintenance of, its business in a safe, efficient and business-like manner and in accordance with its memorandum and articles of association or other constitutional documents, Good Industry Practice (taking its Business as a whole), the Finance Documents and the UK Holdco/Anglian Water Loan and, in the case of Anglian Water, the Instrument of Appointment and the WIA;
  - (e) to comply with the terms of the Transaction Documents to which it is a party;
  - (f) to maintain and take all reasonable steps to enforce its rights and exercise its discretions under the Transaction Documents and Tier 2 Material Agreements in accordance with Good Industry Practice;



- (g) to ensure that, save as otherwise agreed by the Security Trustee and each Financial Guarantor save for any Permitted Joint Venture, the corporate ownership structure of the Anglian Water Services Financing Group (other than the ownership or Control of Anglian Water Services Holdings Ltd) remains as at the date of the Common Terms Agreement;
- (h) so far as permitted by applicable law and regulatory requirements, to execute all such further documents and do all such further things as the Security Trustee (acting reasonably) may consider necessary to give effect to the Finance Documents;
- (i) (A) to take all such action as the Security Trustee may reasonably require for the purpose of perfecting, protecting and preserving the rights of the Security Trustee under the Security Documents and the Security Interests under the Security Documents; and (B) to take all actions as the Security Trustee may require, following the making of any acceleration, cancellation or demand under the Intercompany Loan Arrangements or the termination of, or prepayment of the rentals relative to, the leasing of the Equipment in each case after the occurrence of a Default for facilitating the exercise of the rights of the Security Trustee under the Security Documents and/or the realisation of any Security Interests under the Security Documents; and (C) to use all reasonable endeavours to receive acknowledgments of assignment from such counterparties as the Security Trustee may nominate;
- (j) not to incur any Financial Indebtedness other than Permitted Financial Indebtedness or, in the case of Anglian Water, indebtedness under Permitted Volume Trading Arrangements (Permitted Financial Indebtedness will include indebtedness incurred under the Intercompany Loan Arrangements, any Finance Document, Treasury Transactions entered into in accordance with the Hedging Policy, the Local Authority Loan and any further indebtedness which complies with certain conditions);
- (k) not to enter into any amalgamation, demerger, merger, consolidation or reconstruction other than (in the case of Anglian Water) a Permitted Joint Venture, or otherwise as agreed by the Security Trustee and each Financial Guarantor;
- (l) not to (i) acquire or invest, other than Permitted Acquisitions, Authorised Investments and Permitted Joint Ventures; or (ii) establish any subsidiary (other than as set out in the Common Terms Agreement) or any joint venture other than a Permitted Joint Venture without the prior written consent of the Security Trustee and each Financial Guarantor;
- (m) not to, or to permit any Permitted Joint Venture to, be a creditor in respect of any Financial Indebtedness or issue any guarantee or indemnity in respect of the obligations of any other person except for (A) credit or indemnity provided under any Finance Document (B) any loan made under the Intercompany Loan Arrangements (C) any loan provided to Anglian Water subordinated to the Authorised Credit Facilities on terms acceptable to the Security Trustee (D) any guarantee in the Finance Documents (E) the UK Holdco/Anglian Water Loan (F) single loans by Anglian Water to employees of less than £250,000 (indexed) or loans by Anglian Water to employees in aggregate less than £750,000 indexed; (G) other loans by Anglian Water in aggregate of less than £500,000 (indexed) not falling in (A) to (F) above and (H) in the case of Anglian Water Permitted Volume Trading Arrangements and, in each case (other than for paragraph (B)), provided that no Default or Potential Trigger Event is continuing at the time any such credit or loan or guarantee is proposed to be made or issued;
- (n) not to change its memorandum or articles of association or other constitutional documents in a way which would be reasonably likely to have a Material Adverse

Effect or otherwise prejudice the Security Interests created pursuant to the Security Documents without the prior written consent of the Security Trustee;

- (o) not to propose any resolution for, or agree to any material amendments to, variation, modification, waiver, suspension, revocation, termination of any Material Agreement save in accordance with the Outsourcing Policy without the prior written consent of the Security Trustee;
- (p) not to enter into any Treasury Transaction other than Hedging Agreements entered into in accordance with the Hedging Policy;
- (q) except for a Permitted Tax Loss Transaction, not to enter, without the consent of the Security Trustee and each Financial Guarantor, into any arrangements with any other company or person (other than a taxation authority in respect of the taxation liabilities of such Obligor or any other Obligor) relating to tax;
- (r) not to compromise or settle any claim, litigation or arbitration without prior notification to the Security Trustee if any such compromise or settlement would be reasonably likely to have a Material Adverse Effect;
- (s) (A) to promptly obtain, maintain and comply with the terms of all applicable laws, regulations and orders and obtain and maintain all governmental and regulatory consents, licences, authorisations and approvals (including the Instrument of Appointment) necessary for the conduct of its business, for entry into and performance of the Finance Documents, and for the leasing of the Equipment, as a whole in accordance with Good Industry Practice and (B) to do nothing which would lead to the termination, suspension or revocation of any such consents, licences, authorisations and approvals, in each case where such failure would be reasonably likely to have a Material Adverse Effect;
- (t) to maintain separate bank accounts;
- (u) to use reasonable endeavours to comply in all material respects with all laws and regulations to which it is subject;
- (v) to pay all taxes and other outgoings prior to penalties being incurred unless payment of those taxes is being contested in good faith by appropriate means which permit the deferral of payment and/or an adequate reserve has been set aside for payment of those taxes;
- (w) not to create or allow to exist any Security Interest on the Equipment or any of its present or future revenues or assets other than Permitted Security Interests; or
- (x) not to (A) (i) sell, transfer or otherwise dispose of any of its assets on terms where it is or may be leased to or re-acquired or acquired by a member of the Anglian Water Services Financing Group other than (in the case of the Issuer or Anglian Water) pursuant to a Finance Lease; or (ii) sell, transfer or otherwise dispose of any of its receivables (other than Permitted Book Debt Disposals); or (iii) purchase any asset on terms providing for a retention of title by the vendor or on conditional sale terms or on terms having a like substantive effect to any of the foregoing except for assets acquired in the ordinary course of its business carried on in the normal course, in each case, in circumstances where the transaction is entered into primarily as a method of raising Financial Indebtedness or of financing the acquisition of an asset nor (B) enter into any such transaction in (A) above in circumstances where the transaction is not entered into primarily as a method of raising finance to the extent that the consideration in respect of such sales, leases, transfers or disposals is not received in cash payable in full at the time or exceeds an amount of 0.13 per cent. of RAV in aggregate at any time;
- (y) not to dispose of all or any part of the Equipment or its undertaking, revenues, business or assets other than a Permitted Disposal or Permitted Joint Venture;

- (aa) not to change its tax residence from the United Kingdom;
  - (bb) not to (A) redeem, repurchase, defease, retire or repay any of its share capital or resolve to do so; (B) issue any shares which by their terms are redeemable or convertible or exchangeable for Financial Indebtedness; or (C) issue any share capital to any person, other than where any such action or transaction; (i) is in furtherance of a Restricted Payment and the amount of the Restricted Payment is permitted to be paid pursuant to the Finance Documents or (ii) is expressly allowed under the Finance Documents or (iii) has received the prior written consent of the Security Trustee and each Financial Guarantor; and
  - (cc) other than as a result of Permitted Emergency Action (in which case Anglian Water shall use reasonable endeavours to ensure that all contracts entered into will be on an arm's length basis, although Anglian Water will not be required to obtain alternative competitive quotes), not to enter into any arrangement or contract with any person otherwise than on an arm's length basis save as has been disclosed or unless expressly permitted under the Finance Documents.
- (ii) Additionally, each of Anglian Water Services Holdings Ltd and Anglian Water Services Overseas Holdings Ltd has undertaken:
- (a) not to: (aa) carry on or transact any business or other activity other than (A) ownership of the shares in members of the Anglian Water Services Financing Group held by it on the Effective Date; (B) the giving of guarantees in accordance with the Finance Documents entered into by it on the Effective Date; and (C) the performance of obligations required under the UK Holdco/Anglian Water Loan or the Finance Documents; (bb) own any asset or incur any liabilities except for the purposes of carrying on that business in accordance with the Finance Documents entered into by it on the Effective Date; (cc) suspend, abandon or cease to carry on its business; (dd) declare, make or pay Restricted Payments otherwise than as permitted under the Finance Documents and the UK Holdco/Anglian Water Loan; or (ee) take any steps to enforce any claims it may have against any other Obligor without the prior written consent of the Security Trustee;
  - (b) not to make any Restricted Payments otherwise than out of monies received by it (directly or indirectly) from Anglian Water which have been properly paid by Anglian Water out of the Distributions Account or as set out under the Common Terms Agreement; and
  - (c) to make a UK Holdco Debt Service Distribution in accordance with those provisions referred to in sub-paragraph (v)(E) of paragraph (iv) below immediately once Anglian Water has made a UK Holdco Debt Service Distribution.
- (iii) Each of Anglian Water, Anglian Water Services Holdings Ltd and Anglian Water Services Overseas Holdings Ltd has further undertaken to maintain at least 3 non-executive directors who are not employees or directors of any member of the AWG Group (other than the Obligors) on its board of directors and ensure that, at all times, the directors of any member of the AWG Group (other than the Obligors) do not constitute a majority of the executive directors (subject to temporary vacancies arising out of exceptional circumstances).
- (iv) Additionally, Anglian Water has undertaken, *inter alia*:
- (a) to ensure that the nature of its business is limited to the Business;
  - (b) to conduct its Regulated Business in the name of Anglian Water only and to ensure that separation from the AWG Group is maintained at all times by holding Anglian Water out as a separate entity, correcting any misunderstanding as to identity and using stationery, invoices and cheques separate from any other person or entity;

- (c) not to permit, agree to or recommend any suspension or the abandonment of all or a material part of the operation of its Business unless such suspension or abandonment is in accordance with its Instrument of Appointment;
- (d) if it exceeds the Permitted Non-Statutory Business Limits, to dispose of or reduce all or part of its Permitted Non-Statutory Business within six months so that the Permitted Non-Statutory Business Limits are complied with at the next Calculation Date;
- (e) to comply in all material respects with the Instrument of Appointment;
- (f) not to agree to any amendment or variation of the Instrument of Appointment which would reasonably be expected to have a Material Adverse Effect (without the prior written consent of the Security Trustee);
- (g) to comply with applicable relevant environmental laws and environmental approvals applicable to it, where failure to do so would be reasonably likely to have a Material Adverse Effect;
- (h) as soon as reasonably practicable upon becoming aware of the same, notify the Security Trustee of: (A) any environmental claim that is current or, to the best of its knowledge and belief, is threatened; or (B) any facts or circumstances which will or are reasonably likely to result in an environmental claim being commenced or threatened against it, which, in either case if substantiated, is reasonably likely either to have a Material Adverse Effect or result in any material liability for a Finance Party;
- (i) to effect and maintain those insurances in connection with its Business as are set out in the Common Terms Agreement;
- (j) to take all reasonable action to safeguard and maintain such present and future rights in accordance with intellectual property rights necessary for its Business including observing all covenants and stipulations relating thereto and obtaining all necessary registrations;
- (k) (A) to comply with the Outsourcing Policy which shall become effective on and from the Effective Date and apply it to each Outsourcing Agreement and Capex Contract entered into by Anglian Water (to the extent that it is not entered into pursuant to or under an Existing Framework Agreement) on and from the Effective Date; (B) during the period from the Effective Date until the commencement of the AMP4 Period that all outsourcing is carried out in accordance with Good Industry Practice; (C) subject to (A), to procure that any Outsourcing Agreement and Capex Contract entered into on and from the Effective Date complies with the Public Procurement Rules and the Outsourcing Policy; (D) where an Emergency is continuing, to use its best endeavours to rectify such Emergency (any Permitted Emergency Action will not breach the Outsourcing Policy); (E) to procure that on the commencement of the AMP4 Period, all Existing Framework Agreements (other than Extended Outsourcing Agreements) are terminated or brought into compliance with the Outsourcing Policy; (F) not to materially alter, amend or modify any Extended Outsourcing Agreement without the consent of the Security Trustee and each Financial Guarantor; and (G) to at all times use Good Industry Practice in exercising its rights and performing its obligations under any Extended Outsourcing Agreement;
- (l) to ensure it has adequate financial and management resources to enable it to discharge its core obligations under the Instrument of Appointment and under the Transaction Documents and, in respect of performance obligations which are either passed on to a Contractor or a Permitted Joint Venture or outsourced, it has retained sufficient control to discharge its obligations under the Instrument of Appointment and under the Transaction Documents;

- (m) following receipt of notice of termination of the Instrument of Appointment, Anglian Water must use its reasonable endeavours to ensure that subject to its obligations under the WIA: (A) a Transfer Scheme is agreed between Anglian Water, the transferee and the Director General by a date no less than 2 years prior to the expiration of such notice; and (B) any such Transfer Scheme will not be prejudicial to the interests of the Secured Creditors;
- (n) to use all reasonable endeavours to ensure that the Security Trustee is joined in the consultation process with the Director General if Anglian Water becomes subject to any Transfer Scheme;
- (o) subject to its obligations under the WIA, not to agree to any Transfer Scheme without the consent of the Security Trustee and each Financial Guarantor;
- (p) to ensure that there are no agreements in force or corporate resolutions passed which call for the present or further issue or allotment of, or grant to any person other than Anglian Water Services Overseas Holdings Ltd, the right (whether conditional or otherwise) to call for the issue or allotment of any share (or equivalent) loan note or loan capital of Anglian Water (including an option or right of pre-emption or conversion);
- (q) in the event that the counterparty to the Local Authority Loan commences proceedings for the winding up of any Obligor, to repay such Local Authority Loan in full, no later than 3 days after the commencement of such proceedings;
- (r) in the event that it breaches any of its non-monetary performance obligations under any Existing Finance Lease and such breach would be reasonably likely to have a Material Adverse Effect and has not been remedied or waived, to, within 10 Business Days of becoming aware of such breach, give notice to the relevant Existing Finance Lessor of such breach and prepay all applicable termination sums or rental payable under such Existing Finance Lease upon which the leasing of any and all Equipment under such Existing Finance Lease will terminate immediately and, subject to the terms of the STID, to comply with certain clauses of the Existing Finance Leases as if the relevant Existing Finance Lessor had already served notice of the termination of the leasing of the relevant Equipment on Anglian Water;
- (s) in the event it breaches any of its non-monetary obligations under any Existing Finance Lease and such breach would not be reasonably likely to have a Material Adverse Effect, to indemnify the relevant Existing Finance Lessor in respect of any liabilities suffered or incurred by reason of such breach and if it fails to provide such indemnification (within 60 days of receiving written notice from such Existing Finance Lessor giving written notice and demanding payment), to prepay all rental payments payable under the relevant Existing Finance Lease as if such breach had had a Material Adverse Effect and sub-paragraph (r) above applied;
- (t) except for any Existing Joint Ventures and certain joint venture proposals made by Anglian Water to which both the Security Trustee gives its consent in accordance with the procedure and on the terms set out in the Common Terms Agreement (the Security Trustee's consent only to be given if it is satisfied, *inter alia*, that the liabilities capable of being incurred by Anglian Water as a result of the implementation of the joint venture proposal will not be materially prejudicial to the Secured Creditors and that the net disposal of any asset or right pursuant to the relative joint venture proposal and all net revenues arising from the joint venture proposal are paid to the Receipts Account) and the consent of each Financial Guarantor, not to be unreasonably withheld, has been given, not to enter into any joint venture or other arrangements with other persons whereby the losses and/or profits arising from any activity are incurred by Anglian Water or shared with that other person save where those arrangements are permitted or contemplated by the Outsourcing Policy, or;

- (u) to execute and do all such assurances, acts and things as the Security Trustee may request for perfecting or protecting any security intended to be created under or pursuant to the Security Documents (including, for the avoidance of doubt, any security over any assets or rights which are to form part of the property pursuant to any Permitted Joint Venture);
- (v) to only:
  - (A) pay Customer Rebates at a time when no Event of Default is subsisting and only to the extent it has funds available in the Customer Payment Account;
  - (B) pay any Distribution at a time when no Event of Default is subsisting and only to the extent it has funds available in the Distributions Account;
  - (C) transfer monies to the Distributions Account or Customer Payment Account at any time: (i) when no Default is subsisting and each representation which repeats is correct; (ii) after a duly constituted board meeting has been held approving the declaration of such Distribution; (iii) during the period of 45 days after the date upon which a compliance certificate or interim compliance certificate has been delivered (and an interim compliance certificate must (if issued) be issued within 45 days after the end of any month to which an unaudited profit and loss account has been drawn and as at which an unaudited balance sheet has been produced and must be accompanied by those financial statements and must certify the financial ratios set out therein as at the most recently occurring Calculation Date up to the date of those financial statements). Further the amount that may be transferred shall be limited to an amount equal to the aggregate balance of the Receipts Account and the Payment Account after payment of all prior amounts in accordance with the order set out in the cash management provisions of the CTA (summarised in 7.6.5, “Debt Service Payment Account” below) on the 31 March or 30 September to which that compliance certificate relates; or (in the case of a transfer within 45 days after delivery of an interim compliance certificate) the date of the accounts to which that interim compliance certificate relates, and then only provided that on the day of such transfer:
    - (a) no drawings are outstanding under the Liquidity Facilities, other than Standby Drawings;
    - (b) the transfer is to take place within 45 days after delivery to the Security Trustee of a compliance certificate;
    - (c) two directors of Anglian Water have certified to the Security Trustee that:
      - (i) no Trigger Event is continuing unremedied;
      - (ii) in respect of any Calculation Date falling prior to 31 March 2004 the Senior RAR is less than or equal to 0.86:1 and in respect of any Calculation Date falling after that date, the Senior RAR is less than or equal to 0.85:1 (in each case) for each Test Period in respect of the most recently occurring Calculation Date (after deducting the proposed payment from available cash);
      - (iii) no Default persists or will result from the payment and the representations which repeat are, and will following such payment, remain correct provided that if such Default arises as a result of a notice to terminate the Instrument of Appointment having been served then such Default shall be deemed to be cured if an independent financial adviser shall have certified to the Security Trustee that a Transfer Scheme

or other satisfactory security has been established that will not be materially prejudicial to the interests of Class A Debt Providers or Class B Debt Providers (as the case may be); and

- (iv) to the extent that the payment is to be made to the Distributions Account to enable a Special Distribution to be made or paid, the Senior RAR and Class A RAR as adjusted to take account of that payment do not exceed levels 0.015 below those figures in paragraph (c)(ii) (in the case of the Senior RAR) above and the Trigger Event ratio level set out in paragraph (i)(b) (in the case of Class A RAR) of 7.5.7, “*Trigger Events*”, respectively.
- (D) the criteria listed in paragraphs (v)(A) to (C) above will also apply to payments of Subordinated Debt;
- (E) make a UK Holdco Debt Service Distribution quarterly each year and then only provided that the following conditions are met:
- (a) no Default is subsisting or will result from such payment and each representation which repeats is correct and will, following such payment, remain correct;
  - (b) the payment is made by way of dividend declared and paid in an amount in each financial year equal to such amount as will ensure that Anglian Water Services Overseas Holdings Ltd receives a net amount equal to the amount that it will be required to declare and pay by way of dividend to ensure that Anglian Water Services Holdings Ltd receives a net payment equal to all sums due and payable by Anglian Water Services Holdings Ltd to Anglian Water under the UK Holdco/Anglian Water Loan;
  - (c) Anglian Water Services Overseas Holdings Ltd declares, makes and pays the dividend referred to in (b) above and Anglian Water Services Holdings Ltd fulfils its payment obligations then due under the UK Holdco/Anglian Water Loan on a same day basis with Anglian Water’s payment referred to in (b) above;
  - (d) the payment is made from the Payment Account to the Account of Anglian Water Services Overseas Holdings Ltd at the Account Bank in London subject to the Account Bank having received irrevocable instructions (A) from Anglian Water Services Overseas Holdings Ltd to transfer such sums immediately upon receipt to the Account of Anglian Water Services Holdings Ltd at the Account Bank in London; and (B) from Anglian Water Services Holdings Ltd to transfer such sums immediately upon receipt into the Account to the Payment Account; and
  - (e) all transfers of monies between the Accounts referred to in (d) above occur simultaneously;
- (w) to comply with the obligations to provide information under any surveillance letter with a Financial Guarantor or any Authorised Credit Facility;
- (x) to ensure that a facility in an amount not less than the Maximum Early Redemption Amount to fund the payment of Early Redemption Amounts will continue to be available to be drawn by the Issuer as Permitted Financial Indebtedness under a Finance Document at all times until:
- (i) the day after the last day on which the Early Redemption Event may occur or,

- (ii) if the Early Redemption Event occurs, the payment of all Early Redemption Amounts;
  - (y) to assist with the syndication of any Authorised Credit Facility; and
  - (z) to ensure its pension provisions comply with certain ring-fencing requirements.
- (v) Additionally, Anglian Water and the Issuer have undertaken, *inter alia*:
  - (a) to maintain a rating of the Class A Debt and Class B Debt and a shadow rating of Class A Wrapped Debt with any two of the Rating Agencies;
  - (b) to agree to co-operate with the Rating Agencies in connection with any reasonable request for information in respect of the maintenance of a shadow rating or rating and with any review of its business which may be undertaken by one or more of the Rating Agencies after the date of the Common Terms Agreement;
  - (c) to ensure that there are installed and maintained accounting, management information, financial modelling and cost control systems which are of such a standard which can produce the information required within the time set out in the Finance Documents and procure that there are maintained books of account and other records adequate to reflect fairly and accurately its financial condition, the results of its operations and to provide the reports required to be delivered pursuant to the Finance Documents;
  - (d) to authorise the Auditors to communicate directly with the Security Trustee at such time as such parties may reasonably require (and whilst any Default is outstanding at any time) regarding its accounts and operations and furnish to the Security Trustee a copy of such authorisation, subject to the Auditors' agreement to communicate at such time and upon agreed conditions;
  - (e) to inform the Security Trustee of any change to the Auditors, as soon as reasonably practicable;
  - (f) to only replace the Auditors without the prior written approval of the Security Trustee if the replacement Auditors are a firm of independent public accountants of international standing; and
  - (g) not to change its financial year end without the prior written consent of the Security Trustee such consent not to be refused if Ofwat requires the relevant financial year to be changed in which case Anglian Water will change the financial covenant calculations in such manner as the Security Trustee deems necessary to enable such calculations to continue to be calculated from the relevant financial statements of Anglian Water.
- (vi) Additionally, the Issuer has undertaken, *inter alia*:
  - (a) not to (A) carry on any business other than the raising of funds to provide debt financing to Anglian Water for the purposes of its Business in accordance with the Finance Documents or any Treasury Transaction in accordance with the Hedging Policy; (B) own any assets or incur any liabilities except as required or permitted pursuant to the Finance Documents; (C) suspend, abandon or cease to carry on its business; or (D) take any steps to enforce any claims it may have against any other Obligor without the prior written consent of the Security Trustee;
  - (b) to enter into the interest rate hedging arrangements contemplated in the Hedging Policy, in accordance with the terms of the Hedging Policy;
  - (c) to ensure that (A) no more than 20 per cent. of its aggregate nominal outstanding Financial Indebtedness shall fall due for scheduled final repayment within any period of 24 consecutive months; and (B) no more than 40 per cent. (increased proportionately to the extent that the period from one Periodic Review to the next Period Review is greater than 5 years) of its aggregate nominal outstanding Class A



Debt shall fall due for scheduled repayment within the period from one Periodic Review to the next Periodic Review;

- (d) to use all reasonable endeavours to procure the admission of all listed Bonds for trading on the London Stock Exchange, or such other stock exchange approved by the dealers under the Programme Agreement and the Bond Trustee, and to maintain such admission until none of the relevant listed Bonds is outstanding;
- (e) upon receiving a written request from the Bond Trustee, to deliver to the Bond Trustee a certificate of the Issuer setting out *inter alia* details of the aggregate principal amount outstanding under the outstanding Bonds purchased by the Issuer and as are held by any person for the benefit of any member of the Anglian Water Services Financing Group, any Financial Guarantor or, so far as the Issuer is aware, any of their respective Affiliates, holding companies and subsidiaries;
- (f) to send or procure to be sent (not less than three days prior to the date of publication) to the Bond Trustee for the Bond Trustee's approval, one copy of each notice to be given to the Bondholders in accordance with the Conditions and not to publish such notice without such approval and, upon publication, send to the Bond Trustee two copies of such notice (such approval, unless so expressed, not to constitute approval for the purpose of Section 21 of the Financial Services and Markets Act 2000 of such notice as an investment advertisement (as therein defined));
- (g) procure that the Principal Paying Agent notifies the Bond Trustee forthwith if it does not, on or before the due date for payment in respect of the Bonds, receive unconditionally the full amount in the correct currency of the monies payable on such due date;
- (h) to forthwith give notice to the Bondholders of payments made after their due date to the Principal Paying Agent, the Registrar or the Bond Trustee;
- (i) not less than the number of days specified in the relevant Conditions prior to the redemption or repayment date in respect of any Bond, to give to the Bond Trustee notice in writing of the amount of such redemption or repayment pursuant to the Conditions;
- (j) prior to giving notice to the Bondholders that it intends to redeem the Bonds pursuant to Condition 10(b) (*Early Redemption for Index Reasons*), 10(c) (*Redemption for Tax Reasons*) or 10(d) (*Redemption at the Option of the Issuer (Issuer Call)*), provide such information to the Bond Trustee and the Financial Guarantors as the Bond Trustee and the Financial Guarantors require in order to satisfy themselves of the matters referred to in those Conditions;
- (k) to promptly give notice to the Bond Trustee and to the Security Trustee (A) if it is required by law to effect a deduction or withholding of tax in respect of any payment due in respect of any Bonds listed on a recognised stock exchange within the meaning of Section 841 of the Income and Corporation Taxes Act 1988; or (B) if a Hedge Counterparty is required to make a deduction or withholding of tax in respect of any payment due under the relevant Hedging Agreement; or (C) if it would not be entitled to relief for tax purposes, in any jurisdiction in which it carries on business or is resident for tax purposes, for any material amount which it is obliged to pay under the Finance Documents and which is or has been assumed in the Anglian Water Business Financial Model to be available for relief for tax purposes, and in each case, take such action as may be required by the Bond Trustee and Security Trustee in respect thereof;
- (l) while any of the Bonds remain outstanding, to give notice, or procure that notice is given, to each of the Rating Agencies of (A) any proposed amendment to the Finance Documents other than ones that the Bond Trustee considers to be of a formal, minor or technical nature or made to correct a manifest error or necessary

or desirable for clarification; (B) the Bonds of any Series being repaid in full; (C) the termination of the appointment of the Cash Manager; (D) the appointment of a replacement Bond Trustee or Security Trustee or the appointment of any new or replacement Agents; (E) any Default; (F) the delivery of an Enforcement Notice; (G) the occurrence of any Anglian Water Change of Control; and (H) the occurrence of any UK Holdco Change of Control;

- (m) to observe and comply with its obligations, and use all reasonable endeavours to procure that the Agents observe and comply with all their obligations, under the Agency Agreement and procure that the Registrar maintains the Register and notify the Bond Trustee immediately if it becomes aware of any material breach or failure by an Agent in relation to the Bonds;
- (n) to give not less than 14 days' prior notice to the Bondholders of any future appointment or any resignation or removal of any Agent or of any change by any Agent of its specified office;
- (o) if, before an Interest Payment Date for any Bond, it becomes subject generally to the taxing jurisdiction of any territory or any political sub-division thereof or any authority therein or thereof having power to tax other than or in addition to the United Kingdom, to notify (immediately upon becoming aware thereof) the Bond Trustee of such event and enter into a deed supplemental to the Bond Trust Deed, the Existing Bond Trust Deeds or the assumption agreement in relation to the USPP 2001 Bonds entered into, on, or around the Effective Date, with the substitution for (or, as the case may be, the addition to) the references therein to the United Kingdom of references to that other or additional territory to whose taxing jurisdiction, or that of a political subdivision thereof or any authority therein or thereof, the Issuer becomes subject as aforesaid, such supplemental deed also to modify Condition 10(c) or any equivalent provision of the Existing Bonds or the USPP 2001 Bonds so that such Condition shall make reference to that other or additional territory; and
- (p) to notify the Bond Trustee of any amendment to the Programme Agreement and not agree to any such amendment prior to the delivery of a legal opinion to the Security Trustee if so required.

#### **7.5.6 Financial Covenants**

- (i) Anglian Water has undertaken, *inter alia*:
  - (a) to deliver, with each compliance certificate and each Investors Report, a statement confirming that it has calculated each of the following ratios as at the Calculation Date immediately prior to the date of delivery of that compliance certificate, specifying the results of such calculations and providing a short summary of the manner in which these ratios have been calculated:
    - (A) a Class A ICR for each Test Period;
    - (B) a Senior PMICR for each Test Period;
    - (C) a Class A PMICR for each Test Period;
    - (D) a Senior Average PMICR;
    - (E) a Class A Average PMICR;
    - (F) a Senior RAR for each Test Period;
    - (G) a Class A RAR for each Test Period;
    - (H) the ratio of Net Cash Flow minus Capital Maintenance Expenditure to Class A Debt Interest;

- (b) at each Periodic Review and on making each IDOK application, to apply to the Director General for a price determination which in the reasonable opinion of the Anglian Water directors would allow, at a minimum, a credit rating in the A category to be achieved and maintained for the Class A Unwrapped Debt and a shadow rating in the A category to be achieved and maintained for the Class A Wrapped Debt, in each case such credit rating or shadow credit rating to be from at least two of the Rating Agencies;
  - (c) to apply to the Director General for an IDOK when permitted under the Instrument of Appointment (or use any other means available to apply for an IDOK):
    - (A) in all circumstances which are appropriate in accordance with Good Industry Practice;
    - (B) if the Class A PMICR for any Test Period up to and including the Date Prior is, or is projected to be, less than 1.3:1;
    - (C) if the Senior RAR for any Test Period up to and including the Date Prior is, or is projected to be, equal to or greater than 0.9:1;
    - (D) if an event has occurred which has caused or which is likely to cause a material reduction in its current or projected Net Cash Flow,
 provided that any such application is consistent with prudent management;
  - (d) to levy charges to customers which, together with other available amounts, are as far as possible sufficient, within the constraints of the current price control framework, to enable Anglian Water to meet its operational, investment and financial obligations on a timely basis under the Instrument of the Appointment and its obligations in respect of Financial Indebtedness.
- (ii) The Issuer has further undertaken to maintain:
- (a) Debt Service Reserve Liquidity Facilities available for drawing which (when aggregated with all amounts (including the value of any Authorised Investments) standing to the credit of the Debt Service Reserve Accounts) are not less than the amount of interest (including Lease Reserve Amounts and adjusted Lease Reserve Amounts) payable on its Class A Debt and Class B Debt for the next succeeding 12 month period; and
  - (b) an O&M Reserve Facility available for drawing which when aggregated with amounts standing to the credit of the O&M Reserve Account amount to not less than 10 per cent. of Projected Operating Expenditure and Capital Maintenance Expenditure for the next succeeding 12 month period as forecast in the Anglian Water Business Financial Model.

### 7.5.7 Trigger Events

The Common Terms Agreement also sets out certain Trigger Events. The specific Trigger Events and the consequences which flow from the occurrence of those events (the “Trigger Event Consequences”, as described more particularly in 7.5.8, “*Trigger Event Consequences*” below) are summarised below.

The occurrence of any of the following events will be a Trigger Event:

(i) **Financial Ratios**

On any date when any of the following ratios are calculated in accordance with the Common Terms Agreement to breach the relevant level specified below (reach a “**Trigger Event Ratio Level**”) as at the most recently occurring Calculation Date:

- (a) the Senior RAR for any Test Period is estimated to be more than 0.9:1;
- (b) the Class A RAR for any Test Period is or is estimated to be more than 0.75:1;

- (c) the Senior PMICR for any Test Period is or is estimated to be less than 1.1:1;
- (d) the Class A PMICR for any Test Period is or is estimated to be less than 1.3:1;
- (e) the Senior Average PMICR is or is estimated to be less than 1.2:1; or
- (f) the Class A Average PMICR is or is estimated to be less than 1.4:1.

(ii) **Credit Rating Downgrade**

- (a) The shadow credit rating of any Class A Wrapped Debt given by any two of the Rating Agencies falls to BBB, Baa2 or BBB or below or any Obligor is placed on credit watch with negative implications and it is reasonably likely that such rating given by such Rating Agencies will fall to such levels;
- (b) the credit rating of any Class A Unwrapped Debt by any two of the Rating Agencies falls to BBB, Baa2 or BBB respectively or below or any Obligor is placed on credit watch with negative implications and it is reasonably likely that such rating given by such Rating Agencies will fall to such levels;
- (c) the shadow credit rating of the Class B Wrapped Debt by any two of the Rating Agencies falls below investment grade or any Obligor is placed on credit watch with negative implications and it is reasonably likely that such rating given by such Rating Agencies will fall to such levels; or
- (d) the credit rating of the Class B Unwrapped Debt by any two of the Rating Agencies falls below investment grade or any Obligor is placed on credit watch with negative implications and it is reasonably likely that such rating given by such Rating Agencies will fall to such levels.

Each credit rating referred to above is the “**Trigger Credit Rating**” for the relevant Class of Bonds.

(iii) **Debt Service Payment Account Shortfalls**

The failure to maintain the required credit balance in the Debt Service Payment Account on the required day and within one Business Day of being notified of any shortfall.

(iv) **Material Deviation in Projections**

On any Calculation Date, the estimated actual capital expenditure over any five year period between Periodic Reviews exceeds the capital expenditure for that period assumed by the Director General in the last Periodic Review (adjusted to take account of any subsequent IDOK and Out-turn Inflation) in respect of Anglian Water by 10 per cent. or more.

In each case, deviations resulting from variances in real construction prices from assumed construction prices or additional capital expenditure incurred or to be incurred in respect of items for which Anglian Water is entitled to make an application for an IDOK shall be ignored for the purposes of determining whether the 10 per cent. threshold deviation level has been breached.

(v) **Liquidity for Capital Expenditure and Working Capital**

If, as at any Calculation Date, the aggregate of (i) Anglian Water’s operating cash flows including monies standing to the credit of the Payment Account and the Receipts Account available or forecast to be available to meet capital expenditure and working capital requirements for the next Test Period; (ii) Authorised Credit Facilities (excluding Liquidity Facilities) available to be drawn in the next 12 month period; and (iii) all amounts standing to the credit of the Capex Reserve Account are less than Anglian Water’s (a) forecast capital expenditure projected for the next 12 month period; (b) forecast working capital requirements projected for the next 12 month period; and (c) the maximum total amount of Financial Indebtedness which is or is projected to be outstanding during the next succeeding 12 month period which falls within paragraph (e) of the definition of Permitted Financial Indebtedness.

(vi) **Drawdown on Debt Service Reserve Liquidity Facilities and O&M Reserve Facility**

- (a) If, at any time, the aggregate of all amounts available for drawing under any Debt Service Reserve Liquidity Facility and all amounts standing to the credit of the Debt Service Reserve Accounts is less than an amount equal to the next 12 months' interest (or in the case of the Finance Leases, Lease Reserve Amounts or adjusted Lease Reserve Amounts) payable in respect of Class A Debt and Class B Debt (although it will not be a Trigger Event if it is triggered as a direct result of a banking error and remedied by such amount being repaid within 3 Business Days without such repayment being funded by a further drawing under a Debt Service Reserve Liquidity Facility).
- (b) The Issuer draws down under the O&M Reserve Facility or withdraws funds from the O&M Reserve Account to pay its maintenance costs and not, in the case of the O&M Reserve Facility, just in order to fund the O&M Reserve Account.

(vii) **Enforcement Order**

An Enforcement Order (as defined under the WIA) is issued under Part II, Chapter 11 of the WIA against Anglian Water which would have a Material Adverse Effect if not complied with.

(viii) **Circumstances leading to a Special Administration Order**

Any indication arising from notices and/or correspondence issued by, or during correspondence with, the Director General or any other circumstance of which Anglian Water is aware that would reasonably be expected to lead to an application by the Director General or the Secretary of State for a Special Administration Order to be made in respect of Anglian Water.

(ix) **Termination of Instrument of Appointment**

The giving of a notice to terminate the Instrument of Appointment under the WIA.

(x) **Event of Default**

An Event of Default is continuing.

(xi) **Material Entity Event**

- (a) A Material Entity Event occurs: (A) in relation to a Tier 1 Material Agreement or a Contractor and/or Anglian Water under a Tier 1 Material Agreement and which continues unremedied for 60 days (other than a Material Entity Event under sub-paragraph (i) 7.5.11(i), "*Material Entity Events*" below which continues unremedied for 45 days or (ii) a Material Entity Event which is capable of remedy under sub-paragraphs (ii) or (iii) of 7.5.11, "*Material Entity Events*" below which continues unremedied for 30 days) from the date from which Anglian Water could be reasonably expected to become aware of such Material Entity Event; or (B) in relation to a Tier 2 Material Agreement or a Contractor and/or Anglian Water under a Tier 2 Material Agreement which continues unremedied for six months from the date from which Anglian Water could be reasonably expected to become aware of such Material Entity Event;
- (b) During the period from the Effective Date until the commencement of the AMP4 Period, a Material Entity Event occurs in respect of a Tier 1 Agreement pursuant to sub-paragraph (iv), (v), (vi), (vii) or (viii) of 7.5.11, "*Material Entity Events*" which is capable of remedy and which continues unremedied for 60 days.

unless in either case, the relevant Contractor has been replaced in accordance with the Outsourcing Policy.

(xii) **Referral**

A referral is made under sub-paragraph 14.3 of Condition B in Schedule 2 (Shipwreck) to the Instrument of Appointment (or any successor or equivalent paragraph) as a result of any adverse event.

(xiii) **Audit Qualification**

The Auditors qualify their report on any audited Statutory Accounts of any member of the Anglian Water Services Financing Group in a manner which causes the Security Trustee to believe that the financial ratios calculated in accordance with the Common Terms Agreement may not reflect the true position of Anglian Water.

(xiv) **Adverse Governmental Legislation**

The commencement of the final reading of draft legislation in the House of Lords or the House of Commons (whichever occurs later) of legislation relating to or impacting upon Relevant Undertakers (as that term is defined in the WIA) and such legislation could if enacted reasonably be expected to lead to a breach of the financial ratios referred to in 7.5.7(i), “*Financial Ratios*” above or cause a material deviation as set out in 7.5.7(iv), “*Material Deviations in Projections*” above, in each case taking into account any actions available to Anglian Water to mitigate the same.

(xv) **Modification or Replacement of Instrument of Appointment**

Within three months of an announcement setting out clear proposals by Ofwat for the modifications or replacement of the Instrument of Appointment which, if implemented, could reasonably be expected to have a Material Adverse Effect and a timetable for the implementation of such proposals, Anglian Water has not obtained confirmation from Ofwat that the proposed modification or replacement is not expected to be implemented or is expected to be implemented in a form which is not reasonably expected to have a Material Adverse Effect.

(xvi) **Conduct of Business**

The Permitted Non-Statutory Business Limits are breached.

(xvii) **Breach of Outsourcing Policy**

Anglian Water fails duly to perform or comply with its obligations as required under the Outsourcing Policy (other than as a result of Permitted Emergency Action) and fails to remedy such breach within 90 days of Anglian Water becoming aware of such breach.

(xviii) **No Rating Confirmation on Change of Control after Permitted Demerger**

At any time after a Permitted Demerger a person acquires Control of Anglian Water Services Holdings Ltd or there is any change in the identity of the person who Controls Anglian Water Services Holdings Ltd and a Rating Confirmation on Change of Control has not been obtained in relation to that change of Control.

### 7.5.8 Trigger Event Consequences

Following the occurrence of a Trigger Event and at any time until such Trigger Event has been waived by the Security Trustee, remedied in accordance with Trigger Event Remedies (see 7.5.9, “*Trigger Events Remedies*” below) or otherwise remedied to the satisfaction of the Security Trustee, the provisions set out below will apply:

(i) **No Restricted Payments**

No Obligor may make Restricted Payments and, in respect of Customer Rebates, if these have not yet been implemented, Anglian Water must stop their implementation and must not declare any Customer Rebates.

(ii) **Further Information and Remedial Plan**

(a) Anglian Water must provide such information as to the relevant Trigger Event (including its causes and effects) as may be requested by the Security Trustee.

- (b) Anglian Water must discuss with the Security Trustee its plans for appropriate remedial action and the timetable for implementation of such action. Anglian Water and the Security Trustee may agree a Remedial Plan (with the agreement of the Security Trustee not to be unreasonably withheld or delayed) and any agreed Remedial Plan must then be implemented by Anglian Water.

(iii) **Independent Review**

- (a) The Security Trustee may (acting on the instructions of the Majority Creditors), commission an Independent Review to be undertaken on the timetable stipulated by the Security Trustee. The Independent Review will be conducted by technical advisers to the Security Trustee appointed from time to time or such other person as the Security Trustee may decide.
- (b) The Independent Review will examine the causes of the relevant Trigger Event and recommend appropriate corrective measures.
- (c) Each of the Issuer and Anglian Water must co-operate with the person appointed to prepare the Independent Review including providing access to its books and records and personnel and facilities as may be required for those purposes.

(iv) **Consultation with Ofwat**

The Security Trustee shall be entitled to discuss the relevant Trigger Event and any Remedial Plans with Ofwat at any time.

(v) **Appointment of additional Non-Executive Directors**

If the relevant Trigger Event has not otherwise been remedied or waived within six months from the date of its occurrence or such longer period as the Security Trustee, each Financial Guarantor and Anglian Water may agree in a Remedial Plan, the Security Trustee will be entitled to procure the appointment of additional non-executive directors to the board of Anglian Water provided that the additional non-executive directors appointed by the Security Trustee under this paragraph do not constitute a majority of the board of Anglian Water.

(vi) **Appointment of Additional Directors**

No Obligor may make any additional appointments to the board of any member of the Anglian Water Services Financing Group other than to replace directors upon dismissal, retirement, sudden resignation, death or temporary vacancies unless the Security Trustee and each Financial Guarantor agrees.

In respect of any of the Trigger Event Consequences described above which requires the Security Trustee to exercise its discretion, it must do so upon instructions of the relevant Majority Creditors and any reference to reasonableness and reasonable time will be interpreted accordingly. The Security Trustee is entitled to assume that no Trigger Event has occurred unless informed otherwise.

Even if unremedied, a Trigger Event by itself will not constitute an Event of Default.

### **7.5.9 Trigger Event Remedies**

At any time when the Issuer or Anglian Water (as the case may be) believes that a Trigger Event has been remedied by virtue of any of the following, it shall serve notice on the Security Trustee to that effect, and the Security Trustee must respond within 10 days (or such longer period as it may reasonably stipulate within 5 Business Days of receipt of notice from the Issuer or Anglian Water (as the case may be) to certify that the Issuer or Anglian Water (as the case may be) believes the relevant Trigger Event to have been remedied) confirming that the relevant Trigger Event has, in its reasonable opinion, been remedied or setting out its reasons for believing that such Trigger Event has not been remedied (in which case, such event shall continue to be a Trigger Event until such time as the Security Trustee is reasonably satisfied that the Trigger Event has been remedied).

The following constitute remedies to the Trigger Events:

(i) **Financial Ratios**

The occurrence of a Trigger Event referred to in paragraph 7.5.7(i) of “*Trigger Events*” above shall be remedied if, on any date when the relevant ratio or ratios are calculated in accordance with the Common Terms Agreement such ratio or ratios come within the relevant level or levels specified below as at the most recently occurring Calculation Date:

- (a) the Senior RAR for each Test Period is or is estimated to be less than 0.9:1;
- (b) the Class A RAR for each Test Period is or is estimated to be less than 0.75:1;
- (c) the Senior PMICR for each Test Period is or is estimated to be greater than 1.1:1;
- (d) the Class A PMICR for each Test Period is or is estimated to be greater than 1.3:1;
- (e) the Senior Average PMICR is or is estimated to be greater than 1.2:1; or
- (f) the Class A Average PMICR is or is estimated to be greater than 1.4:1.

(ii) **Credit Rating Downgrade**

The occurrence of a Trigger Event referred to in paragraph 7.5.7(ii) of “*Trigger Events*” above shall be remedied if the credit rating of the relevant class of debt given by any two of the Rating Agencies is above the Trigger Credit Rating or the credit watch is removed and the credit rating of relevant class of debt given by any two of the Rating Agencies remains above the Trigger Credit Rating.

(iii) **Debt Service Required Payment Shortfall**

The occurrence of a Trigger Event referred to in paragraph 7.5.7(iii) of “*Trigger Events*” above will be remedied if payment of the required amount is paid into the Debt Service Payment Account.

(iv) **Material Deviation in Projections**

The occurrence of a Trigger Event referred to in paragraph 7.5.7(iv) of “*Trigger Events*” above will be remedied if the deviations referred to in that paragraph, on any subsequent date, are less than 10 per cent.

(v) **Liquidity for Capital Expenditure and Working Capital**

The occurrence of a Trigger Event referred to in paragraph 7.5.7(v) of “*Trigger Events*” above will be remedied if on any subsequent date the amounts referred to in sub-paragraphs (i) to (iii) of that paragraph are in aggregate equal to or greater than the aggregate of the amounts referred to in sub-paragraphs (a) to (c) of that paragraph.

(vi) **Drawdown on Debt Service Reserve Liquidity Facility and O&M Reserve Facility**

- (a) The occurrence of a Trigger Event referred to in paragraph 7.5.7(vi)(a) of “*Trigger Events*” above will be remedied if the amount available for drawing under a Debt Service Reserve Liquidity Facility when aggregated with all amounts standing to the credit of the relevant Debt Service Reserve Account is restored to the required level.
- (b) The occurrence of a Trigger Event referred to in paragraph 7.5.7(vi)(b) of “*Trigger Events*” above will be remedied if the amount available for drawing under the O&M Reserve Facility, when aggregated with all amounts standing to the credit of the O&M Reserve Account is restored to the required level.



(vii) **Enforcement Order**

The occurrence of a Trigger Event referred to in paragraph 7.5.7(vii) of “*Trigger Events*” above will be remedied if Anglian Water has complied with the terms of the relevant Enforcement Order to the reasonable satisfaction of the Security Trustee or if the Enforcement Order has been effectively withdrawn or if, in the opinion of the Security Trustee (acting reasonably), the relevant fine will not have a Material Adverse Effect or that the Instrument of Appointment will not be terminated.

(viii) **Circumstances leading to a Special Administration Order**

The occurrence of a Trigger Event referred to in paragraph 7.5.7(viii) of “*Trigger Events*” above will be remedied if (a) a Special Administration Order is not made within six months of the relevant Trigger Event occurring or (b) the Security Trustee is reasonably satisfied that a Special Administration Order will not be made in respect of Anglian Water.

(ix) **Termination of Instrument of Appointment**

The occurrence of a Trigger Event referred to in paragraph 7.5.7(ix) of “*Trigger Events*” above will be remedied by agreement by Anglian Water to the extent such Transfer Scheme requires any implementation prior to the termination of the Instrument of Appointment of a Transfer Scheme which is reasonably satisfactory to the Security Trustee.

(x) **Event of Default**

The occurrence of a Trigger Event referred to in paragraph 7.5.7(x) of “*Trigger Events*” above will be remedied if the Event of Default is remedied to the reasonable satisfaction of the Security Trustee.

(xi) **Material Entity Event**

The occurrence of a Material Entity Event referred to in paragraph 7.5.7(xi) of “*Trigger Events*” above will be remedied:

- (a) if it is remedied to the satisfaction of the Security Trustee and each Financial Guarantor;
- (b) if the Contractor has been replaced in accordance with the Outsourcing Policy; or
- (c) upon the acceptance by the Security Trustee and each Financial Guarantor of a Remedial Plan for as long as it is being complied with in all respects.

(xii) **Referral**

The occurrence of a Trigger Event referred to in paragraph 7.5.7(xii) of “*Trigger Events*” above will be remedied if:

- (a) the financial ratios set out in paragraph 7.5.7(i) of “*Trigger Events*” above are continuing to be complied with in the absence of any determination or forecast of the determination of the Director General; or
- (b) the Director General has made a determination that restores the financial ratios referred to in (xii)(a) above to the level specified in paragraph 7.5.7(i) of “*Trigger Events*” above.

(xiii) **Audit Qualification**

The occurrence of a Trigger Event referred to in paragraph 7.5.7(xiii) of “*Trigger Events*” above will be remedied if the Security Trustee is satisfied that such qualification does not affect the veracity of the financial ratios calculated in accordance with the Common Terms Agreement or Anglian Water produces a further set of audited Statutory Accounts which are not qualified.

(xiv) **Adverse Governmental Legislation**

The occurrence of the Trigger Event referred to in paragraph 7.5.7(xiv) of “*Trigger Events*” above will be remedied if the draft bill fails to become an act of parliament or becomes an act in a form which will not cause a breach of the financial ratios set out in paragraph 7.5.7(i) above or the financial ratios are otherwise reinstated to the Trigger Event Ratio Levels as referred to in paragraph 7.5.7(i) of “*Trigger Events*” above or the Director General has confirmed that the capital expenditure which would otherwise have led to a material deviation as referred to in paragraph 7.5.7(iv) of “*Trigger Events*” above is allowable under adjustments to the RAV.

(xv) **Modification or Replacement of Instrument of Appointment**

The occurrence of a Trigger Event referred to in paragraph 7.5.7(xv) of “*Trigger Events*” above will be remedied if an independent expert on behalf of the Security Trustee determines that the modifications to the Instrument of Appointment or, as the case may be, the replacement licence or licences to be granted to Anglian Water will or do contain equivalent terms which permit Anglian Water to carry on its water and sewerage business substantially as carried on as of the Effective Date taking into account any changes in the regulatory environment since the Effective Date and in the opinion of the Security Trustee such terms will not be reasonably likely to:

- (a) have a Material Adverse Effect; or
- (b) result in a breach of the financial ratios as referred to in paragraph 7.5.7(i) “*Financial Ratios*” above.

(xvi) **Conduct of Business**

Within 6 months of the date of the occurrence of the Trigger Event referred to in paragraph 7.5.7(xvi) of “*Trigger Events*” above, Anglian Water disposes of all or part of the Permitted Non-Statutory Business so that the Permitted Non-Statutory Business Limits will be complied with as at, and for the period ending on, the next Calculation Date.

(xvii) **Breach of Outsourcing Policy**

The occurrence of the Trigger Event referred to in paragraph 7.5.7(xvii) of “*Trigger Events*” above will be remedied if Anglian Water takes such action as necessary so that it is in compliance with the Outsourcing Policy.

(xviii) **No Rating Confirmation on Change of Control after Permitted Demerger**

The occurrence of a Trigger Event referred to in paragraph 7.5.7(xviii) of “*Trigger Events*” above will be remedied if a Rating Confirmation on Change of Control is obtained or any downgrade as is referred to in the definition of “Rating Confirmation on Change of Control” which gave rise to that Trigger Event is reversed or such Trigger Event is waived by the Security Trustee and the Initial Financial Guarantor.

In respect of any of the Trigger Event remedies described above which require the Security Trustee to exercise its discretion, it must do so upon instructions of the relevant Majority Creditors, and any reference to reasonableness and reasonable time will be interpreted accordingly.

### **7.5.10 Events of Default**

The Common Terms Agreement contains a number of events of default (the “**Events of Default**”) which will be Events of Default under each Finance Document (other than under the Hedging Agreements). Subject, in some cases, to agreed exceptions, materiality qualifications, reservations of law and grace periods, Events of Default will include (amongst others):

- (i) non-payment of amounts due under the Finance Documents within 3 Business Days of the due date;
- (ii) non-compliance with other obligations under the Finance Documents;

- (iii) material misrepresentation;
- (iv) any Financial Indebtedness not being paid when due (after the expiry of any applicable grace period) or any Financial Indebtedness being declared due and payable prior to its specified maturity as a result of an event of default;
- (v) an Insolvency Event or Insolvency Proceedings in relation to the Obligors other than Anglian Water and in relation to Anglian Water, an insolvency event or insolvency proceedings as set out further in the CTA;
- (vi) Anglian Water transferring the Instrument of Appointment without the Security Trustee's consent or Anglian Water receiving notice that the Instrument of Appointment will be revoked or terminated and a scheme of transfer not being approved by the Secretary of State or the Director General on or before the date falling 2 years prior to the expiration of such notice;
- (vii) the Instrument of Appointment being terminated and not replaced immediately by a further licence on equivalent terms taking into account any changes in the regulatory environment since the Effective Date;
- (viii) insufficient liquidity (from operating cash flows, the Authorised Credit Facilities and the Capex Reserve Account) to meet Anglian Water's forecast capital expenditure and working capital requirements projected for the next 6 month period;
- (ix) attachment, sequestration, distress or execution involving sums in excess of £500,000 (indexed);
- (x) it becoming unlawful for any Obligor to perform its obligations under any Finance Document;
- (xi) an Anglian Water Change of Control occurs;
- (xii) Security becoming invalid, unenforceable or unlawful;
- (xiii) governmental intervention or nationalisation which would be reasonably likely to have a Material Adverse Effect;
- (xiv) an Obligor failing to comply with a judgment involving sums in excess of £500,000 (indexed);
- (xv) other than in the case of a Permitted Lease Termination, an Obligor not having legal power to perform its obligations under the Finance Documents or any obligation of any Obligor under a relevant Finance Document (other than stamp duty indemnities) ceasing to be legal, binding and enforceable and the absence of compliance has a Material Adverse Effect;
- (xvi) Anglian Water failing to comply with its obligations under the Outsourcing Policy (and such failure has a Material Adverse Effect);
- (xvii) an Obligor ceasing to carry on the Business (or any substantial part of the Business) it carries on as at the date of the Common Terms Agreement or as contemplated by the Finance Documents;
- (xviii) litigation being started against an Obligor or its assets or revenues which would be reasonably likely to be adversely determined and, if so adversely determined, would have a Material Adverse Effect;
- (xix) the shadow rating of the Class A Wrapped Bonds or the rating of the Class A Unwrapped Bonds in each case ascribed by two rating agencies being less than the minimum required for Investment Grade;

- (xx) the Class A ICR being less than 1.6:1, the Senior RAR being more than 0.95:1 and/or the ratio of Net Cash Flow minus Capital Maintenance Expenditure to Class A Debt Interest is less than 1:1;
- (xxi) an Obligor amending its memorandum or articles of association (and, in the case of any amendment to Anglian Water’s memorandum or articles, in a manner which is reasonably likely to have a Material Adverse Effect or diminish the Security interest granted in favour of the Security Trustee);
- (xxii) a Material Entity Event (as described in 7.5.11 “*Material Entity Events*” below) occurring which has a Material Adverse Effect.

In respect of each Event of Default requiring any action or discretion on the part of the relevant creditor, the Security Trustee will (save in respect of certain Entrenched Rights and Reserved Matters (see 7.3.18, “*Entrenched Rights and Reserved Matters*” above)) act in accordance with the instructions of the relevant Majority Creditors in accordance with the STID (see 7.3, “*Security Trust and Intercreditor Deed*” above).

Immediately upon the notification to the Security Trustee of an occurrence of an Event of Default, a Standstill Period will commence in accordance with the STID (see 7.3.13, “*Standstill*” above).

#### **7.5.11 Material Entity Events**

The Common Terms Agreement (subject, in some cases to reservations of law and grace periods) provides that each of the following will constitute a Material Entity Event in respect of any Contractor under a Material Agreement or, as the case may be, Anglian Water, to the extent that such Material Entity Event would be reasonably likely to have a Material Adverse Effect:

- (i) failure to pay any amount in excess of £500,000 (indexed) due from the Contractor or Anglian Water unless payment is made within 15 days of an Obligor becoming aware of such failure or save if such payment is being disputed in good faith;
- (ii) any material representation or statement made or deemed to be made by a Contractor or Anglian Water in any Material Agreement is or proves to have been incorrect or misleading in any material respect when made or deemed to be made and such failure, if capable of remedy, is not remedied by the Contractor or Anglian Water within 30 days of it becoming aware that such representation was incorrect or misleading in any material respect;
- (iii) the Contractor or Anglian Water fails duly to perform or comply with any other obligation expressed to be assumed by it in any Material Agreement and such failure, if capable of remedy, is not remedied by such Contractor or Anglian Water, within 30 days of becoming aware of such breach;
- (iv) the Contractor:
  - (A) ceases or suspends generally payment of its debts or publicly announces an intention to do so or is unable to pay its debts as they fall due or is deemed to be insolvent; or
  - (B) commences negotiations with or makes a proposal to any one or more of its creditors concerning its solvency, with a view to the readjustment or rescheduling of any indebtedness;
- (v) an Insolvency Event or equivalent event occurs in relation to a Contractor to a Material Agreement;
- (vi) the Contractor fails to comply with or pay any sum due from it under any judgment or any order made or given by any court of competent jurisdiction when such sums exceed £500,000 (indexed) (or its equivalent) in aggregate at any time except where such judgment is being appealed in good faith to a higher court;
- (vii) any Material Agreement to which the Contractor and Anglian Water is a party or any material obligation purported to be contained therein or the security or credit enhancement intended to be effected in relation to any of the Material Agreements to which it is a party

is repudiated by it or it does or causes to be done any act or thing evidencing an intention to repudiate, abandon, cancel, suspend or terminate any Material Agreement to which it is a party or the security or credit enhancement related thereto or any such material obligation or any such security or subordination effected under any of the Material Agreements to which it is a party or any Material Agreement is not or ceases to be in full force and effect or the legal validity or applicability thereof to any sums due or to become due thereunder is disaffirmed by it or on behalf of it; and

- (viii) the Contractor, Anglian Water or any provider of security or credit enhancement therefor does not have the legal power to perform any of its material obligations under the Material Agreements or, as the case may be, such security or credit enhancement or to own any material assets or to carry on any material part of its business or at any time it is or becomes unlawful for the Contractor, Anglian Water or any provider of security or credit enhancement therefor to perform or comply with any of its material obligations under any Material Agreement or any of the material obligations of the Contractor or any provider of security or credit enhancement thereunder are not or cease to be legal, valid, binding and enforceable.

#### **7.5.12 Conditions Precedent**

The conditions precedent to the issue of further Bonds under the Programme are set out in the CP Document as agreed between, *inter alios*, the Bond Trustee, the Security Trustee and the Obligors.

### **7.6 Cash Management**

#### **7.6.1 Accounts**

In accordance with the Common Terms Agreement, Anglian Water opened and maintains the following Accounts:

- (a) the Receipts Account;
- (b) the Payment Account;
- (c) the Customer Payment Account;
- (d) the O&M Reserve Account;
- (e) the Distributions Account;
- (f) the Capex Reserve Account; and
- (g) the Compensation Account.

It further required the Issuer to open and maintain the following Accounts: (a) the Debt Service Payment Account; (b) the Class A Debt Service Reserve Account; and (c) the Class B Debt Service Reserve Account, and Anglian Water Services Holdings Ltd and Anglian Water Services Overseas Holdings Ltd to each open and maintain a chequing account.

Each of the above accounts together with any bank account of any member of the Anglian Water Services Financing Group are collectively referred to as the “**Accounts**”. Each of the Accounts are held with the Account Bank pursuant to the Account Bank Agreement. Each Obligor agreed in the Common Terms Agreement to comply with the Account Bank Agreement and the provisions of the Common Terms Agreement applying to its Accounts.

#### **7.6.2 Receipts Account**

Under the Common Terms Agreement, Anglian Water agrees to ensure that all of its revenues (excluding any interest or investment income from Authorised Investments) are paid into the Receipts Account or transferred from an existing receipts account to the Receipts Account within one Business Day of receipt. Any payment may be made directly to the Payment Account. Save for refunds of monies received incorrectly and/or compensation payments made to customers in the ordinary course of business, monies credited from time to time to the Receipts Account are transferred periodically at the discretion of Anglian Water to the Payment Account but not otherwise.

### 7.6.3 Payment Account

The Payment Account is the principal current account of Anglian Water through which all operating and capital expenditure or any taxes incurred by Anglian Water and (subject to the terms of the Finance Documents) payments in respect of Financial Indebtedness of the Anglian Water Services Financing Group which are not permitted to be satisfied out of monies in the Debt Service Payment Account are cleared (including any Distributions in respect of the UK HoldCo/Anglian Water Loan). Operating expenditure is funded by cash transfers from the Receipts Account and, if applicable, through direct payments into the Payment Account and through drawings, as and when required and permitted by the Finance Documents, under any Authorised Credit Facility or other Permitted Financial Indebtedness. Capital expenditure is funded out of monies standing to the credit of the Payment Account or Receipts Account or, to the extent such sums are insufficient, out of cash transfers made from the Capex Reserve Account and/or the O&M Reserve Account. On the Effective Date, the balance on the Payment Account was £50,000,000.

Under the Common Terms Agreement, Anglian Water agrees that on the opening of business on the first Business Day of each month until the Discharge Date an amount equal to 1/12th (or, pro rata in the case of the first Test Period) of Anglian Water's Annual Finance Charge for the time being will be transferred from the Payment Account to the Debt Service Payment Account (the "**Monthly Payment Amount**"). If in any month Anglian Water pays an amount into the Debt Service Payment Account to meet payments of AFC Amounts falling due in such month, this will be treated as a prepayment of future Monthly Payment Amounts payable during such Test Period. Accordingly, future Monthly Payment Amounts for that Test Period will be pro rata reduced to reflect such prepayment.

The Annual Finance Charge is calculated by Anglian Water annually on 31 March of each year (or, if such day is not a Business Day, the immediately preceding Business Day) and details included in the next following Investors Report (including any adjustments or recalculations thereto).

Anglian Water shall recalculate the Annual Finance Charge and the Monthly Payment Amount if, during the course of any Test Period, there occurs any increase (whether as a result of any increase in the rate of applicable interest, any drawing under any Authorised Credit Facility, any deferral of interest, any upwards adjustment of rentals under any Finance lease, or otherwise) or decrease (whether as a result of any downwards adjustment of rentals under any Finance Lease or any prepayment or repayment of the debt under which the relevant liabilities arise or accrue or otherwise) and shall adjust the Monthly Payment Amount for the remaining months in the relevant Test Period accordingly.

Anglian Water is prohibited from withdrawing any monies in the Payment Account except on account of the following expenditure and then only in the following order (and provided all prior amounts under previous sub-paragraphs have been paid) (i) operating and capital expenditure of Anglian Water and taxes of any Obligor, (ii) payments to the Debt Service Payment Account in respect of the Monthly Payment Amount, (iii) by way of payment of Class A Debt required under section 7.6.5, "*Debt Service Payment Account*", (iv) for the purpose of transferring monies to the Capex Reserve Account or to the Class A Debt Service Reserve Account in respect of Class A Debt as required under section 7.6.5 and/or the O&M Reserve Account (in each case to the extent required to prevent a breach of covenant or Trigger Event under the Common Terms Agreement), (v) by way of payment of Class B Debt required under section 7.6.5, (vi) for the purpose of transferring monies to the Class B Debt Service Reserve Account in respect of Class B Debt as required under section 7.6.5 (to the extent required to prevent a breach of covenant or Trigger Event under the Common Terms Agreement), (vii) from time to time for the purpose of making payments in respect of Financial Indebtedness which are not to be satisfied out of monies in the Debt Service Payment Account (including sums due as a result of a Permitted Hedge Termination and/or a Permitted Lease Termination), (viii) to pay UK HoldCo Debt Service Distributions or (ix) by way of transfer to the Customer Payment Account or Distributions Account provided that the conditions for making such payments as set out in the Common Terms Agreement (as summarised in paragraph (iv)(v) of 7.5.5, "*Covenants – General*" above) have been satisfied.

### 7.6.4 Capex Reserve Account and O&M Reserve Account

Anglian Water may not withdraw any monies from the Capex Reserve Account or the O&M Reserve Account except for the purpose of any transfer to the Payment Account on account of

Anglian Water's forecast capital expenditure (in the case of the Capex Reserve Account) or operating and maintenance expenditure (in the case of the O&M Reserve Account) for the quarter in which such transfer occurs. In no circumstances shall Anglian Water transfer in any quarter any monies from the Capex Reserve Account or the O&M Reserve Account to the Payment Account in excess of Anglian Water's forecast capital expenditure or operating and maintenance expenditure (as the case may be) for that quarter.

The Issuer and Anglian Water have agreed to ensure that the proceeds of any advance under any Authorised Credit Facility for the purpose of funding capital expenditure is lent to Anglian Water under the Issuer/Anglian Water Loan Agreement and is paid directly into the Capex Reserve Account or the Payment Account.

The Issuer and Anglian Water have further agreed to ensure that the proceeds of any advance under the O&M Reserve Facility is lent to Anglian Water under the Issuer/Anglian Water Loan Agreement and is paid directly into the O&M Reserve Account or the Payment Account.

Anglian Water is not entitled to withdraw any monies credited to the O&M Reserve Account to make payment of any capital expenditure or operating and maintenance expenditure unless at the time of such withdrawal there are no funds standing to the credit of the Payment Account or the Receipts Account.

#### **7.6.5 Debt Service Payment Account**

Anglian Water has agreed in the Common Terms Agreement that (i) each transfer of or in respect of the Monthly Payment Amount from the Payment Account and (ii) upon the commencement of a Standstill Period, the aggregate amount then credited to the Customer Payment Account and the Distributions Account will be paid directly into the Debt Service Payment Account.

The Common Terms Agreement provides that, on each Payment Date, monies credited to the Debt Service Payment Account and (to the extent such amount is insufficient) monies credited to the Payment Account and/or the Receipts Account shall be applied by Anglian Water and the Issuer in the following order and that Anglian Water shall repay the Intercompany Loan Arrangements to such extent as is required for the purpose of enabling the following payments ("**Permitted Payments**") to be made in the following order of priority (the "**Payment Priorities**"):

- (i) first (to the extent there are insufficient monies standing to the credit of all other Accounts and/or available for drawing under any Liquidity Facility), in or towards satisfaction of all operating costs and budgeted maintenance costs;
- (ii) second, in or towards satisfaction of the remuneration, costs and expenses of the Security Trustee and the Bond Trustee;
- (iii) third, in or towards satisfaction of, on a pro rata basis: (a) the remuneration, costs and expenses of the Agent Bank, the USPP Paying Agent, each Paying Agent, each Registrar, each Transfer Agent, each Exchange Agent, the Listing Agent and any other agents appointed under the Agency Agreement or otherwise (each an "**Agent**"), the Account Bank under the Account Bank Agreement, each Debt Service Reserve Liquidity Facility Provider under the relevant Liquidity Facility Agreement, the O&M Reserve Facility Provider under the O&M Reserve Facility, each Authorised Credit Provider under the relevant Authorised Credit Facility, the Cash Manager; and (b) the remuneration, costs and expenses of and premia of each Financial Guarantor pursuant to the relevant I&I Agreement;
- (iv) fourth, pro rata according to the respective amounts thereof, in or towards satisfaction of: (a) all amounts of fees, interest and principal (other than any Subordinated Liquidity Facility Amounts) due or overdue to each Debt Service Reserve Liquidity Facility Provider under the relevant Liquidity Facility Agreement; (b) all amounts of fees, interest and principal (other than Subordinated O&M Reserve Facility Amounts) due or overdue to the O&M Reserve Facility Provider under the O&M Reserve Facility; and (c) all amounts of interest and principal due or overdue to each Authorised Credit Provider under the relevant Authorised Credit Facility to the extent that the Financial Indebtedness was incurred to fund a New Money Advance;

- (v) fifth, pro rata according to the respective amounts thereof, in or towards satisfaction of all scheduled amounts payable to each Hedge Counterparty under any Interest Rate Hedging Agreement (subject to paragraphs (vi) and (xv) below);
- (vi) sixth, pro rata according to the respective amounts thereof, in or towards satisfaction of: (a) all amounts of interest, (including the Lease Reserve Amounts and adjusted Lease Reserve Amounts) and commitment commissions due or overdue in respect of the Class A Debt (other than Subordinated Coupon Amounts and Subordinated Authorised Loan Amounts); (b) any amounts (including termination amounts) due and payable to each Hedge Counterparty under any Interest Rate Hedging Agreement (subject to paragraphs (v) above and (xv) below); (c) all scheduled amounts payable to each Hedge Counterparty under any Currency Hedging Agreement and (following termination of a Standstill Period other than due to remedy or waiver by the Majority Creditors of the Event of Default giving rise to the Standstill Period) all amounts payable to each Hedge Counterparty under any Currency Hedging Agreement (subject to paragraph (xv) below); (d) all amounts of underwriting commissions due or overdue in respect of the Class A Debt; and (e) all reimbursement sums (if any) owed to each Financial Guarantor under the relevant I&I Agreement in respect of payments of interest on any Class A Bonds of the relevant Series guaranteed by such Financial Guarantor;
- (vii) seventh, pro rata according to the respective amounts thereof, in or towards satisfaction of: (a) all amounts of principal due or overdue in respect of the Class A Debt (including in respect of Finance Leases, those amounts payable in respect thereof which do not fall within paragraph (vi) above and do not fall due as a result of the operation of any indemnity or fee reimbursement provision of a Finance Lease); (b) all principal exchange amounts due and payable to each Hedge Counterparty under any Currency Hedging Agreement; (c) any termination amounts or other sums due and payable to each Hedge Counterparty under any Currency Hedging Agreement (subject to paragraph (vi) above and paragraph (xv) below); and (d) all reimbursement sums (if any) owed to each Financial Guarantor under the relevant I&I Agreement in respect of payments of principal on any Class A Bonds of the relevant Series guaranteed by such Financial Guarantor;
- (viii) eighth, pro rata according to the respective amounts thereof, in or towards satisfaction of any Make-Whole Amount due and payable on the Class A Debt and any MBIA Make-Whole Amount;
- (ix) ninth, (to the extent required under the Common Terms Agreement) in payment to the Class A Debt Service Reserve Account;
- (x) tenth, (to the extent required under the Common Terms Agreement) in payment to the O&M Reserve Account;
- (xi) eleventh, pro rata according to the respective amounts thereof, in or towards satisfaction of all amounts of: (a) interest and commitment commissions due or overdue in respect of the Class B Debt (other than any Subordinated Coupon Amounts); (b) all amounts of underwriting commissions (other than Subordinated Commissions) due or overdue in respect of the Class B Debt; and (c) all reimbursement sums (if any) owed to each Financial Guarantor under the relevant I&I Agreement in respect of payments of interest on any Class B Bonds of the relevant Series guaranteed by such Financial Guarantor;
- (xii) twelfth, pro rata according to the respective amounts thereof, in or towards satisfaction of: (a) all amounts of principal due or overdue in respect of the Class B Debt; and (b) all reimbursement sums (if any) owed to each Financial Guarantor under the relevant I&I Agreement in respect of payments of principal on any Class B Bonds of the relevant Series guaranteed by such Financial Guarantor;
- (xiii) thirteenth, pro rata according to the respective amounts thereof, in or towards satisfaction of any Make-Whole Amounts due and payable on the Class B Debt;
- (xiv) fourteenth, (to the extent required under the Common Terms Agreement) in payment to the Class B Debt Service Reserve Account;
- (xv) fifteenth, pro rata according to the respective amounts thereof, in or towards satisfaction of: (a) any other amounts (not included in paragraphs (vi) and (vii) above), due and/or overdue



to the Finance Lessors; and (b) any termination payment due or overdue to a Hedge Counterparty under any Hedging Agreement which arises as a result of a default by such Hedge Counterparty or as a result of a downgrade in the credit rating of such Hedge Counterparty;

- (xvi) sixteenth, pro rata according to the respective amounts thereof, in or towards satisfaction of: (a) all Subordinated Liquidity Facility Amounts due or overdue to each Liquidity Facility Provider under the relevant Liquidity Facility Agreement in respect of Class A Bonds; (b) all Subordinated O&M Reserve Facility Amounts due or overdue to the O&M Reserve Facility Provider under the O&M Reserve Facility; (c) all Subordinated Authorised Loan Amounts due or overdue to each Authorised Credit Provider under the relevant Authorised Credit Facility in respect of Class A Debt; (d) any other indemnified amounts due or overdue to each Financial Guarantor under the relevant I&I Agreement in respect of any Class A Bonds of the relevant Series guaranteed by such Financial Guarantor; and (e) any amounts payable in respect of Class A Debt not referred to in other paragraphs of the Payment Priorities;
- (xvii) seventeenth, pro rata according to the respective amounts thereof, in or towards satisfaction of: (a) all Subordinated Liquidity Facility Amounts due or overdue to each Liquidity Facility Provider under the relevant Liquidity Facility Agreement in respect of Class B Bonds; (b) all Subordinated Authorised Loan Amounts due or overdue to each Authorised Credit Provider under the relevant Authorised Credit Facility in respect of Class B Debt; (c) any other indemnified amounts due or overdue to each Financial Guarantor under the relevant I&I Agreement in respect of any Class B Bonds of the relevant Series guaranteed by such Financial Guarantor; and (d) any amounts payable in respect of Class B Debt not referred to in other paragraphs of the Payment Priorities;
- (xviii) eighteenth, pro rata according to the respective amounts thereof, in or towards satisfaction of all Subordinated Coupon Amounts due or overdue in respect of any Class A Bonds;
- (xix) nineteenth, in or towards satisfaction of all Subordinated Coupon Amounts due or overdue in respect of any Class B Bonds;
- (xx) twentieth (to the extent required in the Common Terms Agreement) shall remain in the Debt Service Payment Account.

For so long as a Standstill Event has not occurred or has occurred and has been cured, Anglian Water will, on the date which is seven Business Days prior to each Payment Date (such date, a “**Determination Date**”), determine whether the aggregate amount of monies then credited to the Debt Service Payment Account is at least equal to the aggregate Financial Indebtedness falling due and payable on such Payment Date (such aggregate amount, “**Scheduled Debt Service**”). If the balance on the Debt Service Payment Account is less than the amount of Scheduled Debt Service, then Anglian Water will promptly transfer sums standing to the credit of the Payment Account and/or the Receipts Account to the Debt Service Payment Account. To the extent that the aggregate of all such sums paid or transferred to the Debt Service Payment Account is less than the Scheduled Debt Service, the Issuer shall promptly request a drawing under the Liquidity Facility. Any proceeds raised by the Issuer in accordance with the terms of the Finance Documents (excluding any permitted post closing events) shall be paid under the Intercompany Loan Arrangements by the Issuer to Anglian Water. Amounts raised (a) to fund capital expenditure shall be paid into the Capex Reserve Account, (b) to refinance existing Financial Indebtedness of the Issuer or Anglian Water shall be paid into the Debt Service Payment Account (and to that extent will not require a drawing on the Debt Service Reserve Liquidity Facility) and (c) for any other purposes shall be paid into the Payment Account.

Until such time as a Standstill Event has occurred and remains unremedied, all amounts payable on any Payment Date shall be paid strictly in the order referred to above, to the intent that no amounts falling to be paid under any sub-paragraph may be paid until such time as the amounts falling to be paid on the same date or earlier under each preceding sub-paragraph have been paid in full.

#### **7.6.6 Debt Service Reserve Accounts**

Anglian Water is allowed (subject to and in accordance with the order for payment specified in 7.6.5, “*Debt Service Payment Account*” above) to transfer monies standing to the credit of the Receipts Account or Payment Account to the Class A Debt Service Reserve Account or the Class B Debt Service Reserve Account, as required.

Anglian Water has agreed to procure that on any Payment Date the aggregate of (i) all amounts available for drawing under the Debt Service Reserve Liquidity Facilities; and (ii) all amounts standing to the credit of the Debt Service Reserve Accounts are equal to the next 12 months’ interest forecast to be due on the Financial Indebtedness of the Anglian Water Services Financing Group.

#### **7.6.7 Compensation Account**

- (i) The Common Terms Agreement requires Anglian Water to ensure that:
  - (a) all proceeds of insurance in excess of £1,000,000 (indexed) per claim, receivable by it or to its order (other than in respect of delay in start up, business interruption or anticipated loss in revenue or third party claims) are paid directly into the Compensation Account; and
  - (b) any such amounts which are not paid directly into the Compensation Account are paid into the Compensation Account immediately upon receipt by (or to the order of) Anglian Water; and
  - (c) any amounts required under the terms of the Common Terms Agreement to be deposited into the Compensation Account following a notice of termination from a Hedge Counterparty are so deposited.
- (ii) Subject to paragraph (iii) below, the Common Terms Agreement provides that Anglian Water may only withdraw amounts from the Compensation Account: (A) in the case of monies representing the proceeds of claims under physical loss or damage policies, for application in meeting payments which are due and payable in respect of the restoration, reinstatement or replacement of the asset lost or damaged or in payment of any Class A Debt falling due on the same day as any Permitted Lease Termination arising as a consequence of the loss of such asset; or (B) in the case of monies paid to Anglian Water’s order to be paid direct to a third party on account of whose claim those insurance proceeds are payable, by way of payment to such third party; or (C) in the case of amounts referred to under paragraph (i)(c) above, in meeting termination sums due under the relevant Hedging Agreement; and/or (D) in paying to the Payment Account any amount deposited which is, at any time, in excess of the amount required to be so deposited.
- (iii) If Anglian Water has paid sums to reinstate, restore or replace effects lost or damaged or to meet claims by third parties out of monies withdrawn from the Receipts Account or Payment Account, then the Common Terms Agreement allows Anglian Water to transfer monies representing the proceeds of the claim to the Payment Account.

#### **7.6.8 Customer Payment Account**

Subject to complying with the Common Terms Agreement, Anglian Water is allowed to credit to the Customer Payment Account such amounts as are permitted to be transferred to the Customer Payment Account pursuant to the terms of the Common Terms Agreement and, in particular, pursuant to the provisions thereof dealing with Restricted Payments (see 7.5.5, “*Covenants – General*”, above).

Anglian Water has agreed to ensure that in respect of each Financial Year in which Customers Rebates are given, the balance on the Customer Payment Account is at all times during such Financial Year equal to the Customer Payment Account Required Balance. To the extent that the balance on the Customer Payment Account is at any time greater than the Customer Payment Account Required Balance, Anglian Water shall withdraw from the Customer Payment Account an amount equal to such excess and transfer such amount to the Payment Account.

Subject to the above, Anglian Water is entitled, at any time prior to the occurrence of a Standstill Event, to apply monies credited to the Customer Payment Account in and towards settlement of a Restricted Payment that is a Customer Rebate.

#### **7.6.9 Distributions Account**

The Common Terms Agreement provides that Anglian Water may only transfer amounts from the Payments Account to the Distributions Account strictly in accordance with the provisions of the Common Terms Agreement (and, in particular, in accordance with the covenant dealing with payments into the Distributions Account (see 7.5.5, “*Covenants – General*”, above)).

Anglian Water is able to withdraw amounts properly standing to the credit of the Distributions Account at any time for payment into the Payment Account or, provided no Event of Default is subsisting, for payment for any purpose.

#### **7.6.10 Authorised Investments**

The Common Terms Agreement allows Anglian Water and the Issuer to invest in certain eligible Authorised Investments such part of the amounts standing to the credit of any of the Accounts as is prudent and in accordance with certain provisions set out in the Common Terms Agreement including that deposits constituting Authorised Investments will only be permitted to the extent that the Authorised Investment is with a bank or financial institution which has agreed, that (i) the Authorised Investment is held to the order of Anglian Water; (ii) any payment in respect of the Authorised Investment will be remitted (in full and without any deduction, withholding or retention of any kind, except to the extent required by law) to the Account Bank; (iii) the Authorised Investment is subject to the Security Interests created by the Security Documents; and (iv) it will not exercise, and will hold the Authorised Investment free of, any Security Interest, right of set-off, counterclaim or other interest which it may have.

#### **7.6.11 Cash Management during a Standstill Period**

The arrangements described in “*Debt Service Payment Account*” above shall continue to apply until the occurrence of a Standstill Event. The Common Terms Agreement provides that, following the occurrence of a Standstill Event and for so long as it continues unremedied and provided no Enforcement Action (other than a Permitted Hedge Termination, a Permitted Lease Termination or a permitted share pledge acceleration) has occurred, the Cash Manager shall assume control of the Accounts, pay operating expenditure when it falls due and, on a monthly basis calculate the aggregate of all payments falling to be made during the next following period of 12 months and shall calculate all net revenues received and/or expected to be received over that 12 month period. To the extent that there is a shortfall in the forecast revenues, the Cash Manager shall notionally apply those forecast revenues to each category in the order set out in 7.6.6, “*Debt Service Payment Account*” until the revenue that is forecast to be available is insufficient to meet all of the payments in any sub-paragraph of 7.6.5, “*Debt Service Payment Account*” above (the “**Shortfall Paragraph**”) and shall, in respect of those categories of payment falling within the Shortfall Paragraph, divide the anticipated revenues remaining pro rata between those amounts. Throughout the Standstill Period, any payments falling to be made within a category of payment falling within a Shortfall Paragraph shall be satisfied by a payment of the pro rata share of that payment so calculated and no payments falling in a category which (in accordance with the order of priority set out in 7.6.5, “*Debt Service Payment Account*”) falls after a Shortfall Paragraph shall be made (and the balance of the payments not made shall remain outstanding).

The proceeds of enforcement of the Security which is permitted to be enforced during a Standstill Period will also be applied in accordance with the above Payments Priorities. In circumstances where such enforcement occurs during a Standstill Period or following an Enforcement Action (other than a Permitted Hedge Termination or a Permitted Lease Termination) under the STID the proceeds of enforcement will be applied in accordance with the above Payment Priorities but excluding in these circumstances payments under 7.6.5(i)(ix) and (xiv).

## 7.7 Security Agreement

### 7.7.1 Security

Each Obligor has entered into the security agreement (the “**Security Agreement**”) with the Security Trustee pursuant to which they each guarantee the obligations of each other Obligor under the Finance Documents to the Security Trustee as security trustee for the Secured Creditors and each secure their property, assets and undertakings to the Security Trustee as trustee for the Secured Creditors. The creation, perfection and enforcement of such security is (in respect of the Security granted by Anglian Water) subject to the WIA, the Instrument of Appointment and requirements thereunder. As a result of the restrictions placed upon Anglian Water in respect of the giving of security and the Special Administration procedure contained in the WIA, the value, effect and enforceability of the security granted by Anglian Water is severely limited (see Chapters 6 “*Risk Factors*” and 11 “*Regulation of the Water and Sewerage Industry in England and Wales*” of this Prospectus for a more detailed discussion of these issues). The Security Agreement does, to the extent applicable, incorporate the provisions of the Common Terms Agreement and the STID.

The security constituted by the Security Agreement is expressed to include:

- (i) first fixed charges over:
  - (a) the shares in Anglian Water, Anglian Water Services Overseas Holdings Ltd and the Issuer;
  - (b) each Obligor’s right, title and interest from time to time in and to:
    - (A) any real property interests currently owned by it or acquired after the date of the Security Agreement (other than certain excluded property not exceeding in aggregate £10 million (indexed));
    - (B) the proceeds of disposal of any land;
  - (c) all present and future plant, machinery, office equipment, computers, vehicles and other chattels;
  - (d) its accounts;
  - (e) any intellectual property rights owned by it (excluding immaterial information technology licence agreements);
  - (f) any goodwill and rights in relation to the uncalled capital;
  - (g) each investment;
  - (h) all shares of any person owned by the Obligor including all dividends, interest and other monies payable in respect thereof and all other rights related thereto;
  - (i) all present and future book and other debts and all monies standing to the credit of its accounts and the debts represented thereby;
- (ii) an assignment of each Obligor’s right, title and interest from time to time in and to:
  - (a) the proceeds of any insurance policies (other than motor insurance, employer’s liability insurance and any other third party liability insurance) and all rights related thereto;
  - (b) all Transaction Documents and any other document or agreement to which an Obligor is a party (subject to certain exceptions); and
- (iii) a first floating charge of the whole of the undertaking, property, assets and rights whatsoever and wheresoever present and future of each Obligor,

except that the security does not include any Protected Land (see Section 11.6, “*Protected Land*”) or any of Anglian Water’s other assets, property and rights to the extent, and for so long as, the taking of any such security would contravene the terms of the Instrument of Appointment and requirements thereunder or the WIA.

The security is held on trust by the Security Trustee for itself and on behalf of the Secured Creditors in accordance with and subject to the terms of the STID.

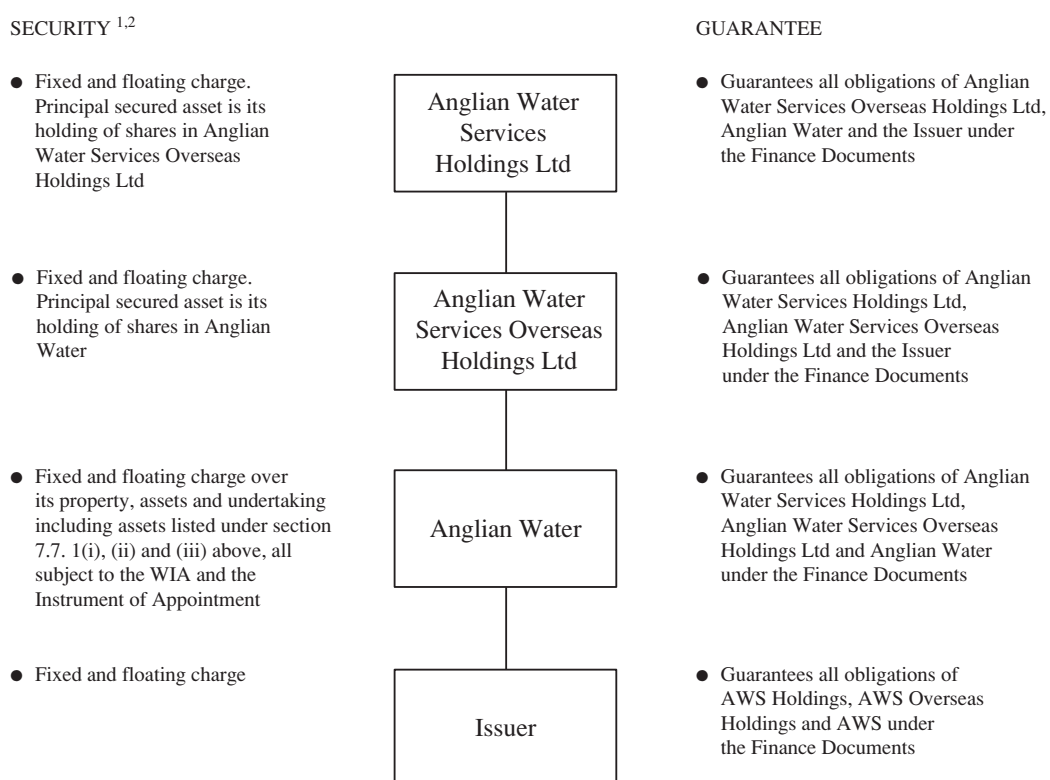
For a description of certain limitations on the ability of Anglian Water to grant security and certain limitations and restrictions on the security purported to be granted, see Section 6.3.1, “*Certain Legal Considerations – Security*” and Section 11.7.1, “*Regulation of the Water and Sewerage Industry in England and Wales – Restrictions on the granting of security*”.

Notice of the creation of the security has not been given initially to customers or to contractual counterparties in respect of contracts (other than certain material contracts) and each charge over land as purported to be granted will take effect in equity only. Accordingly, until notice of the creation of the Security is given to the relevant customers or contractual counterparties or registration is effected with HM Land Registry in respect of registered land or certain other action is taken in respect of unregistered land, to the extent possible any such security or charge may be or become subject to prior equities and/or other legal rights arising in relation thereto.

None of Anglian Water Services Holdings Ltd or Anglian Water Services Overseas Holdings Ltd has or is expected to have any significant assets other than the shares in their respective subsidiaries.

### 7.7.2 Security Structure

The following shows the security provided by the AWG Financing Group in favour of the Security Trustee on behalf of the Secured Creditors:



Notes:

- (1) All security is granted to the Security Trustee as security trustee for the Secured Creditors.
- (2) Anglian Water Services Holdings Ltd, Anglian Water and the Issuer grant all security pursuant to the Security Agreement.

## **7.8 Financial Guarantor Documents**

### **7.8.1 The Bond Policies**

On the Effective Date, MBIA issued in favour of the Bond Trustee (for itself and on behalf of the relevant Class A Wrapped Bondholders) a Bond Policy in respect of the Class A Wrapped Bonds in issue. As the existing MBIA commitment has been fully utilised, no information is included in this Prospectus in relation to MBIA. To the extent that MBIA or any other Financial Guarantors issue Bond Policies in respect of any further Series of Class A Wrapped Bonds and/or Class B Wrapped Bonds, such Bond Policies are expected to be issued by such Financial Guarantor(s) on terms substantially similar thereto.

Upon an early redemption of the relevant Wrapped Bonds or an acceleration of the relevant Wrapped Bonds, MBIA's obligations will continue to be to pay the Insured Amounts as they fall Due for Payment (as defined in MBIA's Bond Policy) on each Payment Date. MBIA will not be obliged under any circumstances to accelerate payment under its Bond Policies. However, if it does so, it may do so in its absolute discretion in whole or in part, and the amount payable by MBIA will be the outstanding principal amount (or pro rata amount that has become due and payable) of the relevant Wrapped Bonds together with accrued interest (excluding always the FG Excepted Amounts). Any amounts due in excess of such outstanding principal amount (and any accrued interest thereon) will not be guaranteed by MBIA or any other Financial Guarantor under any of the Bond Policies.

The Bond Trustee as party to the Bond Policies in issue has, and in respect of Bond Policies to be issued by MBIA or any other Financial Guarantor will have, the right to enforce the terms of such Bond Policies, and any right of any other person to do so is expressly excluded.

### **7.8.2 Insurance and Indemnity Agreements**

On each relevant Issue Date in respect of the Wrapped Bonds, the Issuer and Anglian Water will enter into an insurance and indemnity agreement (each an "**I&I Agreement**") with the relevant Financial Guarantor, pursuant to which the Issuer will be obliged, *inter alia*, to reimburse such Financial Guarantor in respect of the payments made by it under the relevant Bond Policy and to pay *inter alia* any premia and fees and expenses of such Financial Guarantor in respect of the provision of the relevant Bond Policy. Insofar as a Financial Guarantor makes payment under the relevant Bond Policy in respect of Insured Amounts (as defined in such Bond Policy), it will be subrogated to the present and future rights of the relevant Wrapped Bondholders against the Issuer in respect of any payments made.

### **7.8.3 AWG Side Letter**

AWG and MBIA have entered into a letter agreement on the Effective Date under which AWG has agreed that it will not voluntarily cease to have Control of Anglian Water Services Holdings Ltd unless it has first obtained a confirmation from at least two Rating Agencies that such event will not cause the shadow rating of the Class A Wrapped Debt to be downgraded to, or below, BBB+ by Fitch and S&P or, as the case may be, Baa1 by Moody's. AWG also undertook to procure (unless it is unable to do so by reason of any law, judgment, court order, regulation, directive or any regulatory or licence requirement), that any person who gains Control of Anglian Water Services Holdings Ltd will enter into a letter with MBIA on equivalent terms.

## **7.9 Additional Resources Available**

### **7.9.1 Existing Finance Leases**

This section sets out the provisions contained in various Existing Finance Leases that Anglian Water has entered into. The Financing Documents also allow Anglian Water to enter into new Finance Leases in the future, subject to certain limits and provided that any new Finance Lessor accedes to the CTA and the STID.

#### **(i) Supply of Equipment**

Certain leasing companies have acquired equipment and systems and Anglian Water has sold or otherwise procured the supply of certain equipment and systems to leasing companies (or in respect of Equipment which constitutes Fixtures (as defined below) has

been reimbursed for capital expenditure in respect thereof), in each case for the purpose of Anglian Water leasing such equipment and systems from the leasing companies.

The Equipment acquired by or sold or supplied to such leasing companies consists mainly of plant and machinery and other equipment used in the water and sewerage operations of Anglian Water, as well as computer software systems and computer hardware. The Equipment is comprised of movable equipment (“**Movables**”) and fixed equipment (that is Equipment which is so affixed to real estate so as to become part of that real estate as a matter of law (“**Fixtures**”)).

(ii) **Lease Agreements**

Each of the Existing Finance Lessors has leased the Equipment sold or supplied to Anglian Water on the terms and subject to the conditions set out in the following lease agreements between Anglian Water as lessee and the respective leasing company as lessor (each an “**Existing Finance Lease**” and, together, the “**Existing Finance Leases**”). Anglian Water is party to leases with the following Existing Finance Lessors: (a) Mercantile Leasing Company (No. 132) Limited (“**Mercantile**”); (b) D-LAF Limited or Moon Leasing Limited (in its capacity as general partner of Brahms Leasing Limited Partnership (if the D-LAF Existing Finance Lease has been novated to it prior to the Effective Date)) (“**D-LAF**”); (c) Deutsche Bank AG, London Branch (“**Deutsche Bank**”); (d) CSC Computer Sciences Limited; and (e) Barclays Technology Finance Limited (“**DrKW Finance**”) which purchased the interest, and received an assignment of the rights, of Barclays Industrial Finance Limited (“**DrKW Industrial Finance**”) under its Existing Finance Lease (which Existing Finance Lease is also referred to herein as the “**DrKW Industrial Finance Existing Finance Lease**”). The DrKW Finance Existing Finance Lease, together with the DrKW Industrial Finance Existing Finance Lease are referred to as “**DrKW Existing Finance Leases**”.

The existence of the purchase options in the DrKW Existing Finance Leases (see 7.9.1(xi), “*Repossession of Movables on Termination*” below) probably means that these leases are more properly characterised as hire purchase agreements.

In relation to Fixtures, because no title passes to the relevant Existing Finance Lessors (or if it does that title reverts to the landowner on affixation to real estate of the relevant Equipment), Anglian Water and each relevant Existing Finance Lessor has elected to deem that ownership is in that Existing Finance Lessor and that there is a deemed lease of the Fixtures in question.

(iii) **Lease periods**

The primary lease period under the D-LAF Existing Finance Lease is 15 years from the commencement of such lease period and this period is extended, automatically in the case of Movables and at the Existing Finance Lessor’s discretion in the case of Fixtures, for another 35 years. Under the Mercantile Existing Finance Lease the primary period is for 25 years from the lease commencement date and this period may be extended, automatically in the case of Movables and at the Existing Finance Lessor’s discretion in the case of Fixtures for another 25 years. Under the Existing Finance Lease with Deutsche Bank the primary lease period runs from the lease commencement date until 30 March 2005 at which date Anglian Water is entitled to extend the lease period for another 10 years. Under the DrKW Finance Existing Finance Lease the primary lease period is for 49 months, which, subject to early termination, is renewed automatically on expiry for an indefinite period. In the DrKW Industrial Finance Existing Finance Lease the lease periods are 5 years from the lease commencement date in respect of the hardware and 7 years from the lease commencement date in respect of the software.

(iv) **Subject to Common Terms Agreement and STID**

Each Existing Finance Lease has been amended so as to be subject to the CTA. In this way the representations, warranties, covenants and events of default set out in the Common Terms Agreement apply in respect of the Existing Finance Lessors for each Existing Finance Lease. The Existing Finance Leases are also subject to the STID which regulates

the claims of the Existing Finance Lessors against Anglian Water and termination and enforcement rights under the Existing Finance Leases. Certain of the material terms of the Existing Finance Leases (in addition to those incorporated from the CTA) are outlined below (see 7.9.1(vii), “*Anglian Water Obligations*” below).

(v) **Rental**

Anglian Water is obliged to make regular rental payments (“**Rental**”) under each Existing Finance Lease, annually in advance under the Mercantile Existing Finance Lease and the Deutsche Bank Existing Finance Lease, six monthly in advance under the D-LAF Existing Finance Lease and quarterly in advance under the DrKW Existing Finance Leases.

The primary period Rental payable under each of the Existing Finance Leases (except the DrKW Existing Finance Leases) is calculated by reference to a number of assumptions made at the time of execution of the relevant Existing Finance Lease (including a specific assumed rate of interest) and if any such assumption proves to be incorrect, the primary rental payments under the relevant Existing Finance Lease are adjusted to levels that seek to (or if all those rentals have been paid additional rentals or rebates of rental are made in order to) preserve the relevant Existing Finance Lessors agreed after-tax rate of return on its acquisition cost of the Equipment leased under that Existing Finance Lease. The rental payments payable during any secondary period are also set out in the relevant Existing Finance Lease.

The assumptions set out in the Mercantile Existing Finance Lease, the D-LAF Existing Finance Lease and in the Deutsche Bank Existing Finance Lease are the type of tax and financial assumptions customarily found in leases of this kind and include (*inter alia*) matters such as the rate of corporation tax, the rate of writing down allowances, the amount of group relief on tax losses which may be claimed by the lessor and other changes in applicable law or regulation.

Rental under the DrKW Finance Existing Finance Lease is fixed for a minimum period of 49 months from 31 March 2000 and then continues automatically beyond the expiry of the minimum period until terminated in accordance with the DrKW Finance Existing Finance Lease. If Anglian Water continues the DrKW Finance Existing Finance Lease past the minimum period then Anglian Water has to pay a one-off payment of £10. There is no set expiry date beyond the minimum period. Anglian Water may voluntarily terminate the lease of the Systems by payment of a termination payment to the Existing Finance Lessor. The amount of such termination payment is referred to in 7.9.1(x), “*Additional Termination Rights under Existing Finance Leases*”.

Rental under the DrKW Industrial Finance Existing Finance Lease is also fixed although a separate payment is required (i) by Anglian Water to the Existing Finance Lessor if the actual rate of interest (calculated by reference to sterling deposit rates) on DrKW Industrial Finance’s investment balance is greater than the assumed rate (set at 5.7318 per cent. per month) or (ii) by the Existing Finance Lessor to Anglian Water if the actual rate is less than the assumed rate.

Anglian Water will pay any VAT (if payable) due in respect of any payments under the Existing Finance Leases.

(vi) **General Payment Provisions**

Default interest is payable under each Existing Finance Lease in respect of any late payment.

All Rental and other payments under each Existing Finance Lease (other than the DrKW Finance Existing Finance Lease) are required to be made free and clear of, and without withholding or deduction for, tax, if any, applicable to such payments unless such withholding or deduction is required by law. In that event, Anglian Water will be obliged to pay such additional amounts as will result in the receipt by the relevant Existing Finance Lessor of such amount that the relevant Existing Finance Lessor would have received if no such withholding or deduction had been required.



The Existing Finance Leases (other than the DrKW Finance Existing Finance Lease) provide that if the relevant Existing Finance Lessor determines in its absolute discretion that it has received or has been granted a credit against or remission from any tax payable which is attributable to such additional amounts payable by Anglian Water then the Existing Finance Lessor shall reimburse such amount as shall leave the Existing Finance Lessor after such reimbursement in no worse position than the Existing Finance Lessor would have been in if the deduction or withholding had not been required.

(vii) **Anglian Water Obligations**

In addition to the representations and warranties made by Anglian Water, and the covenants applying to Anglian Water, under the CTA, the Existing Finance Leases also impose certain customary finance lease representations, warranties and covenants on Anglian Water.

In particular, Anglian Water is typically required, in accordance with the Existing Finance Leases, although not always in each case, *inter alia*, (1) to keep the Equipment in good repair condition and working order, (2) to ensure the Equipment is used in a skilful and proper manner, (3) to make good all damage to the Equipment and (4) to maintain third party liability and property insurances in respect of the Equipment.

A breach of any of these representations or covenants in an Existing Finance Lease which would be reasonably likely to have a Material Adverse Effect will, to the extent not remedied or waived, oblige Anglian Water to prepay all sums due and payable under the relevant Existing Finance Lease (as outlined above, see 7.5.5 “Covenants – General” paragraphs (iv)I and (s)) and will be subject to the CTA and the STID. If Anglian Water does not make such prepayment in accordance with the CTA and the STID, it will constitute an Event of Default (to the extent not remedied by Anglian Water or waived (upon notice of that event to the Security Trustee) by the Existing Finance Lessor in question) with the result that the Standstill Period will automatically commence.

(viii) **General Indemnities**

Each Existing Finance Lease (other than the DrKW Finance Existing Finance Lease) contains a general indemnity whereby Anglian Water agrees to indemnify the relevant Existing Finance Lessor against, *inter alia*, all losses, and damages (excluding taxes), in any way associated with the transactions contemplated in the relevant Existing Finance Lease other than those arising as a result of (*inter alia*) the wilful misconduct of the relevant Existing Finance Lessor.

Other than the DrKW Finance Existing Finance Lease, each Existing Finance Lease typically (but not in all cases) provides that Anglian Water shall indemnify under the Existing Finance Leases the relevant Existing Finance Lessor against all losses incurred or suffered by it, *inter alia*, in relation to the Equipment or as a result of failure by Anglian Water to comply with its obligations under the relevant Existing Finance Lease.

Under the DrKW Finance Existing Finance Lease, Anglian Water indemnifies the relevant Existing Finance Lessor against, *inter alia*, all losses and damages arising generally out of its acts or omissions.

(ix) **Tax Indemnities**

Under the terms of the Existing Finance Leases (other than the DrKW Finance Existing Finance Lease), Anglian Water is required to indemnify the Existing Finance Lessors for certain tax liabilities arising in relation thereto, either by way of variation of the Rental payment amounts (see 7.9.1(v), “Rental” above) or contractual indemnity payments.

Typically, these indemnities survive any termination of the leasing of the Equipment and the termination of the Existing Finance Leases themselves.

(x) **Additional Termination Rights under Existing Finance Leases**

The Existing Finance Leases contain termination rights on the part of the Existing Finance Lessor in addition to the Events of Default set out in the CTA and those outlined in 7.9.1(vii), “*Anglian Water Obligations*” above. These include: a right to terminate following a total loss of any Equipment (other than in respect of the DrKW Existing Finance Leases where Anglian Water has an option to elect to pay a termination payment or replace the lost Equipment) or illegality (in the case of the Deutsche Bank Existing Finance Lease only). In these circumstances, subject to the terms of the CTA, the STID and the Existing Finance Leases (as amended and supplemented), each Existing Finance Lessor may terminate the leasing of the Equipment under its Existing Finance Lease and charge a termination sum in the circumstances outlined above, save that Anglian Water in each case will not make any payment if (i) an Acceleration of Liabilities has occurred or (ii) a Default Situation is subsisting or would occur as a result of such payment. If Anglian Water fails or is unable to make any prepayment in accordance with the CTA and the STID an Event of Default will arise under the CTA and upon notice of that event to the Security Trustee the Standstill Period will automatically commence.

Anglian Water may voluntarily terminate the leasing of all or part of the Equipment under any Existing Finance Lease and pay, *inter alia*, all Rentals due thereunder in advance of the expiry of the relevant lease period provided that (i) no Acceleration of Liabilities has occurred and (ii) no Default Situation is subsisting or would occur as a result of such payment.

The Existing Finance Leases (other than the DrKW Existing Finance Leases) provide that upon termination, a termination payment becomes payable as calculated pursuant to the financial schedule attached to the relevant Existing Finance Lease or, in the case of the Deutsche Bank Existing Finance Lease, the relevant rental clause. The termination payment payable is calculated by a reference to a number of assumptions which if subsequently proven to be incorrect may give rise to a further payment or a rebate in the future.

In the Existing Finance Leases (other than the DrKW Existing Finance Leases) termination payments may vary according to the termination event which takes place and the date thereof. They are calculated, broadly speaking, by the production of a revised cash flow as at the date of the relevant termination based upon certain assumptions. Broadly the termination payment will be an amount equal to the aggregate of (i) sums due and payable under the relevant Existing Finance Lease and (ii) an amount equal to the balance of the relevant Existing Finance Lessor’s investment in the relevant Existing Finance Lease and so as to preserve the Existing Finance Lessor’s net after-tax return. Additionally the Mercantile Existing Finance Lease and the D-LAF Existing Finance Lease require a termination fee to be paid if termination occurs within a period specified therein.

The DrKW Existing Finance Leases also provide for payment of termination payments to the relevant Existing Finance Lessors upon termination of the leases. The termination payments include (*inter alia*) amounts for all arrears of Rental and sums due and unpaid, a sum equal to the total of all future Rentals which would have fallen due under the relevant Existing Finance Lease (in the case of the DrKW Industrial Finance Existing Finance Lease only during the specified minimum hire period) discounted to the date of termination, and breakage costs.

(xi) **Repossession of Movable on Termination**

To the extent the Existing Finance Leases relate to Fixtures there is no ability to repossess the relevant Equipment but both the Mercantile Existing Finance Lease and the D-LAF Existing Finance Lease provide that, after termination of the hiring of the Equipment for whatever reason, the Existing Finance Lessor may require Anglian Water to dismantle, dispose, or store and maintain until sold, any “Surplus Equipment” (i.e. so much of the Movable as is then no longer required to ensure that the functions of Anglian Water under the WIA may be properly carried out). Upon the termination of the hiring of any Surplus Equipment, and so long as no termination event has occurred (or, if it has occurred, is not continuing or has been remedied) Anglian Water shall at its own expense be entitled and

bound to act as the exclusive sales representative of the Existing Finance Lessor for a period of one year after termination of the hiring of the Surplus Equipment and thereafter as non-exclusive sales representative to find a purchaser of the Surplus Equipment. Following a sale of any Surplus Equipment the Existing Finance Lessor shall rebate (by way of rebate of Rentals) any proceeds of sale (less the Existing Finance Lessor's termination payments and other amounts due) to Anglian Water.

The Deutsche Bank Existing Finance Lease provides that if Anglian Water is not in default of any of its obligations under the lease, Anglian Water shall act as the Existing Finance Lessor's agent for the purpose of selling the Equipment (defined in the lease as the "Goods") (other than any software) after the Existing Finance Lessor has recovered possession of any of the Goods being the subject of a termination. Anglian Water may be entitled to a rebate of Rentals upon a termination of the hiring of Goods provided the Existing Finance Lessor receives such amounts as are required to maintain the agreed rate of return as set out in the Existing Finance Lease.

Pursuant to the DrKW Industrial Finance Existing Finance Lease, upon any termination of the provision of the computerised billing system known as NBS (as the assets are so defined in the DrKW Industrial Finance Existing Finance Lease), or expiry of the lease period, Anglian Water shall immediately return the hardware to the Existing Finance Lessor. Anglian Water has the option to purchase NBS (£10 for hardware and £10 for software). If Anglian Water, does not purchase NBS, then the Existing Finance Lessor is obliged to use all reasonable endeavours to sell it and then if Anglian Water has paid all amounts due to the Existing Finance Lessor, then the Existing Finance Lessor shall pay to Anglian Water as a rebate of Rental so much of the proceeds of sale (less any costs and expenses) received by the Existing Finance Lessor as does not exceed the total of the rental and termination payments paid by Anglian Water.

Pursuant to the DrKW Finance Existing Finance Lease, upon any termination of the provision of the Equipment (defined as the "Systems" in the DrKW Finance Existing Finance Lease), Anglian Water shall immediately return the Systems to the Existing Finance Lessor. Anglian Water also has the option to purchase the Systems for £10. Further, if the option to purchase is not exercised by Anglian Water, the Existing Finance Lessor is obliged to use all reasonable endeavours to sell the Systems. If Anglian Water has paid all amounts due to the Existing Finance Lessor and the Systems are sold, then the Existing Finance Lessor shall pay to Anglian Water as a rebate of Rental so much of the proceeds of sale (less any costs and expenses) received by the Existing Finance Lessor as does not exceed the total of the Rental and termination payments paid by Anglian Water.

(xii) **Insurance and Total Loss**

The Existing Finance Leases (other than the DrKW Existing Finance Leases) provide that Anglian Water is to effect and maintain insurance against all risk of loss of or damage to the Equipment (or, in the case of the Deutsche Bank Existing Finance Lease, against all usual risks). The DrKW Existing Finance Leases provide that Anglian Water shall bear all risk of loss of or damage to the Systems and indemnify the Existing Finance Lessor on demand against such risk.

The Mercantile Existing Finance Lease and the D-LAF Existing Finance Lease provide that Anglian Water shall effect and maintain in full force and effect third party liability insurance cover in respect of all the Equipment in accordance with and to the extent and in the amounts required to comply with good and prudent water industry insurance practice in the United Kingdom.

Upon a total loss of certain items of Equipment, the leasing of such items will terminate and Anglian Water must pay a termination payment (from insurance proceeds or otherwise) within a specified number of business days following such total loss or within a certain number of business days after the date of receipt of insurance proceeds in relation to such Equipment.

Anglian Water bears the full risk of any total loss of or any damage to all or a material part of the Equipment (except in relation to the DrKW Existing Finance Leases where Anglian Water has the option to replace the Systems or pay the Existing Finance Lessor a termination payment).

(xiii) **Related Guarantee**

The payment obligations of Anglian Water under each of the Mercantile Existing Finance Lease and the D-LAF Existing Finance Lease were guaranteed by Anglian Water Plc (now AWG Group Ltd). Each of these guarantees were released and discharged on or before the Effective Date.

(xiv) **Capital Allowances**

The Existing Finance Lessors constitute Secured Creditors and have the benefit of the security package which the Obligors granted under the Security Agreement. Although leading counsel has advised that section 225 of the Capital Allowances Act 2001 (“**Section 225**”) should not apply, there is a risk that the available benefit of the security package could cause Section 225 to apply to the D-LAF Existing Finance Lease and the Mercantile Existing Finance Lease. If Section 225 did apply in this way, the Existing Finance Lessors under those Existing Finance Leases would not be able to claim capital allowances in relation to the capital expenditure they have incurred on the leased Equipment. Under the terms of the relevant Existing Finance Leases, the cost of this inability to claim capital allowances would be passed on to Anglian Water in the form of higher Rentals.

## 7.9.2 The Local Authority Loan

Anglian Water has an outstanding loan of approximately £124,000 from Castle Point Borough Council which has not acceded, and will not be required to accede, to the CTA or the STID.

## 7.9.3 Authorised Loan Facility

The Issuer has entered into a facility agreement (an “**Authorised Loan Facility**”) with an aggregate facility amount of £225,000,000 with the Initial Authorised Credit Provider(s). The Authorised Loan Facility is a revolving credit facility which is available to the Issuer for working capital and capital expenditure requirements from 25 November 2004 until 31 July 2010.

Drawings under the Authorised Loan Facility are subject to various conditions precedent as set out therein, including that no Event of Default or Potential Event of Default is subsisting (in relation to the capital expenditure element of the Authorised Loan Facility only) and no Event of Default is subsisting (in relation to the working capital element of the Authorised Loan Facility) and each repeating representation is correct at the time of requesting and making the drawing.

Interest accrues on any drawing under the Authorised Loan Facility calculated at a daily rate by reference to applicable sterling LIBOR plus a margin and mandatory costs.

The Issuer gave representations and warranties, covenants and undertakings to the Authorised Credit Providers on terms as set out, respectively, in the Common Terms Agreement.

The Events of Default under the Common Terms Agreement apply under the Authorised Loan Facility (see 7.5, “*Common Terms Agreement*” above).

The ability of the Authorised Credit Providers to accelerate any sums owing to them under the Authorised Loan Facility upon or following the occurrence of an Event of Default thereunder is subject to the STID.

The Issuer may enter into further Authorised Credit Facilities on terms similar to those in the Authorised Loan Facility. Each additional Authorised Credit Provider will be given the benefit of the Security and will be required to accede to the STID and the CTA.

## 7.9.4 The Liquidity Facilities

There are three Liquidity Facilities in place, the Debt Service Reserve Liquidity Facilities (as defined below) and the O&M Reserve Facility (as defined below), each of which are maintained

by the Issuer, the proceeds of which are on-lent to Anglian Water under the Intercompany Loan Arrangements.

The Issuer has entered into agreements (each a “**Debt Service Reserve Liquidity Facility Agreement**”), with the Liquidity Facility Providers, establishing liquidity facilities (each a “**Debt Service Reserve Liquidity Facility**”). The Issuer has established Debt Service Reserve Liquidity Facilities in connection with Bonds and other debt issued and incurred.

Under the terms of each Debt Service Reserve Liquidity Facility Agreement, one or more Liquidity Facility Providers provide a 364-day commitment in an aggregate amount specified in each Debt Service Reserve Liquidity Facility Agreement to permit drawings to be made by the Issuer, in circumstances where Anglian Water has or will have insufficient funds available on a Payment Date to pay scheduled interest under the Intercompany Loan Arrangements, to enable the Issuer to make payments due on a Series of Bonds or other Senior Debt (a “**Liquidity Shortfall**”).

The Issuer has also entered into agreements (each an “**O&M Reserve Facility Agreement**”) with one or more Liquidity Facility Providers establishing liquidity facilities (each an “**O&M Reserve Facility**”) proceeds of which are on-lent to Anglian Water to meet Anglian Water’s operating and capital maintenance expenditure requirements to the extent that Anglian Water has insufficient funds available to it to meet these requirements.

Under the terms of the O&M Reserve Facility, one or more Liquidity Facility Providers provide a 364-day commitment in an aggregate amount specified in each such agreement.

Each Liquidity Facility Provider must be a bank which as at the relevant Issue Date has a Minimum Short-Term Rating and a minimum long-term rating at a level of at least “A” from Fitch and S&P and at least “A2” from Moody’s from at least two of the Rating Agencies (the “**Liquidity Facility Requisite Ratings**”). The Initial Liquidity Facility Provider is Barclays Bank PLC.

The Liquidity Facility Provider may be replaced at any time provided that such Liquidity Facility Provider is replaced by a bank with the Liquidity Facility Requisite Ratings and all amounts outstanding to such Liquidity Facility Provider are repaid in full.

Each Debt Service Reserve Liquidity Facility Agreement provides that amounts repaid by the Issuer may be redrawn.

Each Liquidity Facility Agreement provides that if (i) at any time the rating of the relevant Liquidity Facility Provider falls below the Liquidity Facility Requisite Ratings or (ii) the relevant Liquidity Facility Provider does not agree to renew such Liquidity Facility prior to the expiry of the 364-day period, the Issuer will:

- (a) use all reasonable endeavours to replace the relevant Liquidity Facility Provider with a party having the Liquidity Facility Requisite Ratings (whether by way of novation of the relevant Liquidity Facility Agreement or by entering into a new Liquidity Facility Agreement with a party having the Liquidity Facility Requisite Ratings); and
- (b) if a replacement is not made within the relevant time period specified in the relevant Liquidity Facility Agreement be entitled to require such Liquidity Facility Provider to pay into the relevant Liquidity Account or other such agreed account to which such Liquidity Facility relates, an amount equal to the affected party’s undrawn commitment under such Liquidity Facility (a “**Standby Drawing**”).

If the Issuer does not request a renewal of the Liquidity Facility from the relevant Liquidity Facility Provider, (b) above will not apply.

Unless otherwise agreed by the Issuer, the Security Trustee and each Financial Guarantor:

- (a) liquidity in respect of Class A Debt will be applied in making payments in respect of Class A Debt only and liquidity in respect of Class B Debt will be applied in making payments in respect of Class B Debt only; and

- (b) amounts repaid under a Debt Service Reserve Liquidity Facility provide liquidity for Class A Debt to the extent necessary to ensure that the amount available under Debt Service Reserve Liquidity Facilities providing liquidity for Class A Debt and the amount standing to the credit of the Class A Debt Service Reserve Account equals the next 12 months' interest forecast on Class A Debt, with any surplus providing liquidity in respect of Class B Debt.

The Standby Drawing will generally be repayable only if the relevant Liquidity Facility Provider is re-rated with the Liquidity Facility Requisite Ratings or confirmation is received from each of the Rating Agencies that either (i) the terms of a replacement Liquidity Facility or (ii) the absence of any such facility, in each case, as applicable will not lead to a ratings downgrade of the Bonds from the relevant Rating Agencies. The proceeds of the Standby Drawing will be placed in an Account over which security has been granted pursuant to the terms of the Security Agreement.

Interest accrues on any drawing (including a Standby Drawing) made under the Liquidity Facility provided by the Initial Liquidity Facility Provider at a reference rate per annum plus a margin. Under the Liquidity Facility Agreements, the Issuer is also required to pay additional amounts if: (i) a withholding or deduction for or on account of tax is imposed on payments made by it to the relevant Liquidity Facility Provider; or (ii) if the relevant Liquidity Facility Provider suffers an increase in the cost of providing the relevant Liquidity Facility. Drawings under any further Liquidity Facilities will accrue interest subject to the specific terms of the relevant Liquidity Facility Agreement.

Upon the enforcement of the Security pursuant to the STID, all indebtedness outstanding under any Liquidity Facility (other than Subordinated Liquidity Facility Amounts) will rank in priority to the Bonds.

## 7.10 Hedging Agreements

### 7.10.1 Hedging Policy

The Hedging Policy provides that the Anglian Water Services Financing Group must enter into Hedging Agreements in accordance with an agreed Hedging Policy and that the only member of the Anglian Water Services Financing Group that may enter into Hedging Agreements is the Issuer, provided that the Issuer may enter into back-to-back swap arrangements with Anglian Water in respect of Hedging Agreements entered into by the Issuer to hedge the obligations of Anglian Water under the Existing Finance Leases or which are otherwise not directly linked to the raising of new debt under an Authorised Credit Facility. The Hedging Policy, *inter alia*, requires that the Anglian Water Services Financing Group enter into appropriate hedging instruments (with hedge counterparties with appropriate credit ratings) to limit their exposure to currency and interest rate fluctuations and to inflation to a prudent level. It further requires that all Hedging Agreements are entered into or novated under an agreement in the form of the 1992 ISDA Master Agreement (Multicurrency – Cross Border) (an “**ISDA Master Agreement**”) and that the Hedging Agreements provide, *inter alia*, for “*two way payments*” or payments under the “*Second Method*” in the event of an early termination and set out the circumstances in which a Hedge Counterparty may designate an Early Termination Date (as defined in the relevant Hedging Agreement) with respect to the relevant Hedging Agreement. If an Early Termination Date occurs in circumstances where both interest rate hedging transactions and currency hedging transactions are being terminated, amounts payable under interest rate hedging transactions and currency hedging transactions will be treated separately to enable the Issuer to comply with the Payment Priorities. The Anglian Water Services Financing Group is prohibited from entering into hedging transactions for the purpose of speculation or otherwise than in accordance with the agreed Hedging Policy. The Hedging Policy may only be amended by agreement between the Security Trustee and Anglian Water. Subject to such agreement being reached, the Hedging Policy will be reviewed from time to time by the Anglian Water Services Financing Group and amended (subject to Entrenched Rights and Reserved Matters and in accordance with provisions of the STID) as appropriate in accordance with market developments, Good Industry Practice and regulatory developments.

### 7.10.2 Hedging Agreements

Prior to the Effective Date, AWG Group Ltd and Anglian Water entered into certain hedging transactions with the Existing Hedge Counterparties to establish a hedge in relation to currency and interest rate exposures arising under certain debt instruments and the Existing Finance Leases. Anglian Water had also entered into certain additional hedging transactions with the Existing Hedge Counterparties to hedge against the Issuer's interest rate exposure in relation to the Bonds issued on the Effective Date and other Financial Indebtedness to be incurred. The rights and obligations of AWG Group Ltd and Anglian Water under such transactions were either cancelled or novated to the Issuer by AWG Group Ltd or Anglian Water, as the case may be. Payments are made between the Issuer and the Existing Hedge Counterparties under the Existing Hedging Agreements on the relevant Payment Dates.

The Hedge Counterparties are obliged to make payments under the Hedging Agreements without any withholding or deduction of taxes, unless required by law. If any such withholding or deduction is required by law, the Hedge Counterparties are required to pay any such additional amount as is necessary to ensure that the net amount received by the Issuer is equal to the full amount the Issuer would have received had no such deduction or withholding been required. The Issuer makes payments under the Hedging Agreements subject to any withholding or deduction of taxes required by law, but is not required to pay any additional amount to any Hedge Counterparty in respect thereof. However, in either case, if a withholding or deduction is required due to any action by a taxing authority, or change in tax law after the date on which a transaction is entered into, which cannot be avoided, the Hedge Counterparty may terminate the relevant Hedging Agreement.

The Issuer has the right to terminate a Hedging Agreement, in certain circumstances, relating to the relevant Hedge Counterparty (or, if applicable, any Credit Support Provider or Specified Entity (as defined in the relevant Hedging Agreement) relating to it) including: a failure to pay amounts when due, the occurrence of an insolvency event, a breach of a term of the Hedging Agreement or any Credit Support Document (as defined in the relevant Hedging Agreement); a merger without assumption; a default under a Specified Transaction (as defined in the relevant Hedging Agreement); and in the event of Illegality (as defined in the relevant Hedging Agreement).

Other than in certain limited circumstances (set out in paragraphs 9 and 21I of Schedule 8 of the CTA), each Hedge Counterparty's rights to terminate its Hedging Agreement are limited to the following circumstances: (i) a failure by the Issuer to make payments under the Hedging Agreement when due; (ii) certain insolvency-related events with respect to the Issuer, (iii) Illegality (as defined in the relevant Hedging Agreement); (iv) where either the Hedge Counterparty or the Issuer is required to withhold for tax, which cannot be avoided ("Tax Event" as defined in the Hedging Agreements); and (v) a Standstill Period has ended otherwise than in accordance with Clause 13.4(a)(iii) of the STID (and in this event, termination will be automatic).

Pursuant to paragraph 21I of Schedule 8 to the CTA, but only in respect of any Hedging Agreements entered into before the Effective Date or Hedging Agreements entered into on the Effective Date which replace such Hedging Agreements, the Hedge Counterparties are entitled to exercise any right they may have to terminate such Hedging Agreement pursuant to any break clause or right of optional early termination contained in that Hedging Agreement (but not, for the avoidance of doubt, an Event of Default, Tax Event Upon Merger or Credit Event Upon Merger (as such terms are defined in the Hedging Agreement) or as a result of a change in the Instrument of Appointment or in the regulatory status of Anglian Water) provided that:

- (i) no Default is continuing or would result from such termination; and
- (ii) all amounts payable by the Issuer as a result of such termination are capable of being paid out of existing revenues of the Anglian Water Services Financing Group or otherwise out of Permitted Financial Indebtedness.

The Hedging Policy provides that the Issuer may enter into Treasury Transactions with Hedge Counterparties where each relevant Hedge Counterparty has the right to terminate the relevant Treasury Transaction on the tenth anniversary of the effective date of such Treasury Transaction and thereafter no more frequently than at five yearly intervals provided that such right of termination is exercised in accordance with paragraph 9 of Schedule 8 to the CTA. The Issuer has

not and will not enter into any Treasury Transactions for a period in excess of 10 years other than to the extent that at any date the aggregate notional amount and/or currency amounts (as applicable) of relevant Treasury Transactions to which the Issuer is a party and which have unexpired terms in excess of 10 years would not exceed an amount equal to 15 per cent. of RAV in each case as computed in accordance with the Hedging Policy.

Each Existing Hedge Counterparty is a party to the STID and the CTA and its rights (including, in particular, its rights to receive any termination payment) are subject thereto. Accordingly, any termination payment will be paid to a Hedge Counterparty in accordance with the cash management arrangements set out in the CTA and summarised in 7.6, “*Cash Management*”.

In the event that the short-term unsecured and unsubordinated debt obligations of a Hedge Counterparty (or its successor, assignee or transferee) or of its Credit Support Provider (as defined in the relevant Hedging Agreement) (or the successor, assignee or transferee of any such Credit Support Provider) cease to be rated at least as high as P-1 by Moody’s or A-1 by S&P or F-1 by Fitch and, as a result of such downgrade, the then current rating of the Class A Unwrapped Bonds (or if no Class A Unwrapped Bonds are outstanding, the then current shadow rating of the Class A Wrapped Bonds, or if there are no Class A Wrapped Bonds outstanding, the then current rating of the Class B Unwrapped Bonds or, if there are no Class A Bonds and no Class B Unwrapped Bonds outstanding, the then current shadow rating of the Class B Wrapped Bonds) is downgraded or placed under review for possible downgrade by the Rating Agencies, then the relevant Hedge Counterparty will either: (i) provide collateral for its obligations, (ii) arrange for its rights and obligations under the relevant Hedging Agreement to be transferred to an appropriate third party with the required credit ratings; (iii) arrange for the appointment of a co-obligor in respect of the obligations of the relevant Hedge Counterparty or take such other action as will result in the rating of the relevant Bonds then outstanding following the taking of such action being rated no lower than the rating of the relevant Bonds immediately prior to such downgrade; or (iv) take such other action that will result in the rating of the relevant Bonds being maintained or restored to the level they would have been at immediately prior to such downgrade. If the relevant Hedge Counterparty does not take the measures described above, such failure shall constitute an Additional Termination Event with respect to the relevant Hedge Counterparty. The Issuer and the Security Trustee shall endeavour to put into place credit support documentation as may satisfy the Rating Agencies with respect to the operation and management of the collateral provided pursuant to (i) above and enter into such documents as may reasonably be requested by the relevant Hedge Counterparty in connection with the provision of such collateral.

## **7.11 Other Transaction Documents**

### **7.11.1 Account Bank Agreement**

Pursuant to the Account Bank Agreement, the Account Bank agreed to hold the Accounts and operate them in accordance with the instructions of the Cash Manager. The Cash Manager manages the Accounts on behalf of the Anglian Water Services Financing Group pursuant to the Common Terms Agreement (see 7.6, “*Cash Management*” above).

### **7.11.2 Corporate Services Agreement**

Pursuant to a corporate services agreement (the “**Anglian Water Services Overseas Holdings Ltd Corporate Services Agreement**”), Maples and Calder provide certain corporate services to Anglian Water Services Overseas Holdings Ltd.

### **7.11.3 Tax Deed of Covenant**

Under the terms of the Tax Deed of Covenant, each Obligor gave certain representations and covenants as to its tax status and to the effect that it has not taken and, save in certain permitted circumstances, will not take any steps which might reasonably be expected to give rise to a liability to tax for an Obligor which is primarily the liability of another person. AWG covenanted and represented that it had not taken and would not take any steps that might cause the Obligors to breach such covenants and representations.

With a view to avoiding a liability to tax for an Obligor which is primarily the liability of another person, AWG and each Obligor under the Tax Deed of Covenant, incur certain obligations in relation to specified disposal events and any change in tax residence of the Obligors. For example,



the Tax Deed of Covenant provides that if (other than in compliance with an obligation the Obligor incurs under a Finance Document) an Obligor intends to dispose of any of its material assets to another person, AWG can be required, as a condition of that disposal, to deposit an amount in a trust account equal to the estimated tax liability (if any) arising or likely to arise in the Obligor as a result of the disposal. The money deposited could then be used to pay the tax liability of the Obligor if the Obligor failed to pay the liability itself.

## CHAPTER 8

### FORM OF THE BONDS

The Bonds of each Series will be in either bearer form, with or without interest coupons (“**Coupons**”) attached, or registered form, without interest coupons attached. Bearer Bonds will be issued outside the United States in reliance on Regulation S and Registered Bonds will be issued both outside the United States in reliance on the exemption from registration provided by Regulation S and within the United States in reliance on Rule 144A or Regulation D under the Securities Act.

#### **Bearer Bonds**

Each Tranche of Bearer Bonds will be initially issued in the form of either a temporary bearer global bond (a “**Temporary Bearer Global Bond**”) or a permanent bearer global bond (a “**Permanent Bearer Global Bond**”) as indicated in the applicable Final Terms, which, in either case, will be delivered on or prior to the original issue date of the Tranche to a common depository (the “**Common Depository**”) for Euroclear Bank S.A./N.V. as operator of the Euroclear System (“**Euroclear**”) and Clearstream Banking, *société anonyme* (“**Clearstream, Luxembourg**”). Whilst any Bearer Bond is represented by a Temporary Bearer Global Bond and subject to TEFRA D selling restrictions, payments of principal, interest (if any) and any other amount payable in respect of the Bonds due prior to the Exchange Date (as defined below) will be made against presentation of the Temporary Bearer Global Bond only to the extent that certification (in a form to be provided) to the effect that the beneficial owners of interests in such Bearer Bond are not U.S. persons or persons who have purchased for resale to any U.S. person, as required by U.S. Treasury regulations, has been received by Euroclear and/or Clearstream, Luxembourg and Euroclear and/or Clearstream, Luxembourg, as applicable, has given a like certification (based on the certifications it has received) to the Principal Paying Agent.

On and after the date (the “**Exchange Date**”) which is 40 days after a Temporary Bearer Global Bond is issued, interests in such Temporary Bearer Global Bond will be exchangeable (free of charge) upon a request as described therein either for (i) interests in a Permanent Bearer Global Bond of the same Series or (ii) for definitive Bearer Bonds of the same Series with, where applicable, receipts, Coupons and talons attached (as indicated in the applicable Final Terms and subject, in the case of definitive Bearer Bonds, to such notice period as is specified in the applicable Final Terms), in each case against certification of beneficial ownership as described above unless such certification has already been given, provided that purchasers in the United States and certain U.S. persons will not be able to receive definitive Bearer Bonds. The holder of a Temporary Bearer Global Bond will not be entitled to collect any payment of interest, principal or other amount due on or after the Exchange Date unless, upon due certification, exchange of the Temporary Bearer Global Bond for an interest in a Permanent Bearer Global Bond or for definitive Bearer Bonds is improperly withheld or refused.

Payments of principal, interest (if any) or any other amounts on a Permanent Bearer Global Bond will be made through Euroclear and/or Clearstream, Luxembourg against presentation or surrender (as the case may be) of the Permanent Bearer Global Bond without any requirement for certification.

The applicable Final Terms will specify that a Permanent Bearer Global Bond will be exchangeable (free of charge), in whole but not in part, for definitive Bearer Bonds with, where applicable, receipts, Coupons and talons attached upon either (i) not less than 60 days’ written notice from Euroclear and/or Clearstream, Luxembourg (acting on the instructions of any holder of an interest in such Permanent Bearer Global Bond) to the Principal Paying Agent as described therein or (ii) only upon the occurrence of an Exchange Event. For these purposes, “**Exchange Event**” means that (i) an Event of Default (as set out in Schedule 7 of the Common Terms Agreement (as defined in Chapter 9, “*Terms and Conditions of the Bonds*”)) has occurred and is continuing, (ii) the Issuer has been notified that both Euroclear and Clearstream, Luxembourg have been closed for business for a continuous period of 14 days (other than by reason of holiday, statutory or otherwise) or have announced an intention permanently to cease business or have in fact done so and no successor clearing system is available or (iii) the Issuer has or will become subject to adverse tax consequences which would not be suffered were the Bonds represented by the Permanent Bearer Global Bond in definitive form and a certificate to such effect signed by two Directors of the Issuer is given to the Bond Trustee. The Issuer will promptly give notice to Bondholders in accordance with Condition 18 if an Exchange Event occurs. In the event of the occurrence of an Exchange Event, Euroclear and/or Clearstream, Luxembourg (acting on the instructions of any holder of an interest in such Permanent Bearer Global Bond) or the Bond Trustee may give notice to the Principal Paying Agent requesting exchange and, in the event of the occurrence of an Exchange Event as described in (iii) above, the Issuer may also give notice to the Principal Paying Agent requesting exchange. Any such exchange shall occur not later than 45 days after the date of receipt of the first relevant notice by the Principal Paying Agent.

The following legend will appear on all Bearer Bonds which have an original maturity of more than 365 days and on all receipts and interest coupons relating to such Bonds:

“ANY UNITED STATES PERSON WHO HOLDS THIS OBLIGATION WILL BE SUBJECT TO LIMITATIONS UNDER THE UNITED STATES INCOME TAX LAWS, INCLUDING THE LIMITATIONS PROVIDED IN SECTIONS 165(j) AND 1287(a) OF THE INTERNAL REVENUE CODE.”

The sections referred to provide that United States holders, with certain exceptions, will not be entitled to deduct any loss on Bearer Bonds, receipts or interest coupons and will not be entitled to capital gains treatment of any gain on any sale, disposition, redemption or payment of principal in respect of such Bonds, receipts or interest coupons.

Bonds which are represented by a Bearer Global Bond will only be transferable in accordance with the rules and procedures for the time being of Euroclear or Clearstream, Luxembourg, as the case may be.

In the event that a Global Bond is exchanged for definitive Bonds, such definitive Bonds shall be issued in Specified Denomination(s) only. Bondholders who hold Bonds in the relevant clearing system in amounts that are not integral multiples of a Specified Denomination may need to purchase or sell, on or before the relevant Exchange Date, a principal amount of Bonds such that their holding is an integral multiple of a Specified Denomination.

### **Registered Bonds**

The Registered Bonds of each Tranche offered and sold in reliance on Regulation S, which will be sold to non-U.S. persons outside the United States, will initially be represented by a global bond in registered form, without Receipts or Coupons, (a “**Regulation S Global Bond**”). Prior to expiry of the distribution compliance period (as defined in Regulation S) applicable to each Tranche of Bonds, beneficial interests in a Regulation S Global Bond may not be offered or sold to, or for the account or benefit of, a U.S. person save as otherwise provided in Condition 2 and may not be held otherwise than through Euroclear or Clearstream, Luxembourg and such Regulation S Global Bond will bear a legend regarding such restrictions on transfer.

The Registered Bonds of each Tranche may only be offered and sold in the United States or to U.S. persons in private transactions (i) to “qualified institutional buyers” within the meaning of Rule 144A under the Securities Act (“**QIBs**”) or (ii) to “accredited investors” (as defined in Rule 501(a)(1), (2), (3) or (7)) under the Securities Act that are institutions (“**Institutional Accredited Investors**”) who agree to purchase the Bonds for their own account and not with a view to the distribution thereof. The Registered Bonds of each Tranche sold to QIBs will be represented by a global bond in registered form (a “**Rule 144A Global Bond**” and, together with a Regulation S Global Bond, the “**Registered Global Bonds**”).

Registered Global Bonds will either (i) be deposited with a custodian for, and registered in the name of a nominee of, DTC or (ii) be deposited with a common depository for, and registered in the name of a common nominee of, Euroclear and Clearstream, Luxembourg, as specified in the applicable Final Terms. Persons holding beneficial interests in Registered Global Bonds will be entitled or required, as the case may be, under the circumstances described below, to receive physical delivery of definitive Bonds in fully registered form.

The Registered Bonds of each Tranche sold to Institutional Accredited Investors will be in definitive form, registered in the name of the holder thereof (“**Definitive IAI Registered Bonds**”). Unless otherwise set forth in the applicable Final Terms, Definitive IAI Registered Bonds will be issued only in minimum denominations of U.S.\$500,000 and integral multiples of U.S.\$1,000 in excess thereof (or the approximate equivalents in the applicable Specified Currency). Definitive IAI Registered Bonds will be subject to the restrictions on transfer set forth therein and will bear the restrictive legend described in Chapter 15 under “*Subscription and Sale and Transfer and Selling Restrictions*”. The Rule 144A Global Bond and the Definitive IAI Registered Bonds will be subject to certain restrictions on transfer set forth therein and will bear a legend regarding such restrictions.

Payments of principal, interest and any other amount in respect of the Registered Global Bonds will, in the absence of provision to the contrary, be made to the person(s) shown on the Register (as defined in Condition 7) as the registered holder(s) of the Registered Global Bonds. None of the Obligor, any Paying Agent or the Registrar will have any responsibility or liability for any aspect of the records relating to or payments or deliveries made on account of beneficial ownership interests in the Registered Global Bonds or for maintaining, supervising or reviewing any records relating to such beneficial ownership interests.

Payments of principal, interest or any other amount in respect of the Registered Bonds in definitive form will, in the absence of provision to the contrary, be made to the persons shown on the Register on the relevant Record Date (as defined in Condition 8) immediately preceding the due date for payment in the manner provided in that Condition.

Interests in a Registered Global Bond will be exchangeable (free of charge), in whole but not in part, for definitive Registered Bonds without receipts, Coupons or talons attached only upon the occurrence of an Exchange Event. For these purposes, “**Exchange Event**” means that (i) an Event of Default has occurred and is continuing, (ii) in the case of Bonds registered in the name of a nominee for DTC, either DTC has notified the Issuer that it is unwilling or unable to continue to act as depository for the Bonds and no alternative clearing system is available or DTC has ceased to constitute a clearing agency registered under the Exchange Act, (iii) in the case of Bonds registered in the name of a nominee for a common depository for Euroclear and Clearstream, Luxembourg, the Issuer has been notified that both Euroclear and Clearstream, Luxembourg have been closed for business for a continuous period of 14 days (other than by reason of holiday, statutory or otherwise) or have announced an intention permanently to cease business or have in fact done so and, in any such case, no successor clearing system is available or (iv) the Issuer has or will become subject to adverse tax consequences which would not be suffered were the Bonds represented by the Registered Global Bond in definitive form and a certificate to such effect signed by two Directors of the Issuer is given to the Bond Trustee. The Issuer will promptly give notice to Bondholders in accordance with Condition 18 if an Exchange Event occurs. In the event of the occurrence of an Exchange Event, DTC, Euroclear and/or Clearstream, Luxembourg (acting on the instructions of any holder of an interest in such Registered Global Bond) or the Bond Trustee may give notice to the Registrar requesting exchange and, in the event of the occurrence of an Exchange Event as described in (iv) above, the Issuer may also give notice to the Registrar requesting exchange. Any such exchange shall occur not later than 10 days after the date of receipt of the first relevant notice by the Registrar.

#### **Transfer of Interests**

Interests in a Registered Global Bond may, subject to compliance with all applicable restrictions, be transferred to a person who wishes to hold such interest in another Registered Global Bond and Definitive IAI Registered Bonds may, subject to compliance with all applicable restrictions, be transferred to a person who wishes to hold such Bonds in the form of an interest in a Registered Global Bond. No beneficial owner of an interest in a Registered Global Bond will be able to transfer such interest, except in accordance with the applicable procedures of DTC, Euroclear and Clearstream, Luxembourg, in each case to the extent applicable. **Registered Bonds are also subject to the restrictions on transfer set forth therein and will bear a legend regarding such restrictions, see Chapter 15, “Subscription and Sale and Transfer and Selling Restrictions”.**

#### **General**

Pursuant to the Agency Agreement (as defined in Chapter 9, “*Terms and Conditions of the Bonds*”), the Principal Paying Agent shall arrange that, where a further Tranche of Bonds is issued which is intended to form a single Series with an existing Tranche of Bonds, the Bonds of such further Tranche shall be assigned a common code and ISIN and, where applicable, a CUSIP and CINS number which are different from the common code, ISIN, CUSIP and CINS assigned to Bonds of any other Tranche of the same Series until at least the expiry of the distribution compliance period applicable to the Bonds of such Tranche.

For so long as any of the Bonds is represented by a Global Bond held on behalf of Euroclear and/or Clearstream, Luxembourg each person (other than Euroclear or Clearstream, Luxembourg) who is for the time being shown in the records of Euroclear or of Clearstream, Luxembourg as the holder of a particular nominal amount of such Bonds (in which regard any certificate or other document issued by Euroclear or Clearstream, Luxembourg as to the nominal amount of such Bonds standing to the account of any person shall be conclusive and binding for all purposes save in the case of manifest error) shall be treated by the Obligors and their agents as the holder of such nominal amount of such Bonds for all purposes other than with respect to the payment of principal or interest on such nominal amount of such Bonds, for which purpose the bearer of the relevant Bearer Global Bond or the registered holder of the relevant Registered Global Bond shall be treated by the Obligors and their agents as the holder of such nominal amount of such Bonds in accordance with and subject to the terms of the relevant Global Bond and the expressions “**Bondholder**” and “**holder of Bonds**” and related expressions shall be construed accordingly.

So long as DTC or its nominee is the registered owner or holder of a Registered Global Bond, DTC or such nominee, as the case may be, will be considered the sole owner or holder of the Bonds represented by such Registered Global Bond for all purposes under the Bond Trust Deed, the Agency Agreement and such Bonds

except to the extent that in accordance with DTC's published rules and procedures any ownership rights may be exercised by its participants or beneficial owners through participants.

Any reference herein to Euroclear and/or Clearstream, Luxembourg and/or DTC shall, whenever the context so permits, be deemed to include a reference to any additional or alternative clearing system specified in the applicable Final Terms.

So long as the Bonds are represented by a temporary Global Bond or permanent Global Bond and the relevant clearing system(s) so permit, the Bonds shall be tradeable only in principal amounts of at least the Specified Denomination (or if more than one Specified Denomination, the lowest Specified Denomination) provided hereon and integral multiples of the Tradeable Amount provided in the relevant Final Terms.

### **Applicable Final Terms**

*Set out below is the form of Final Terms which will be completed for each Tranche of Bonds issued under the Programme.*

Final Terms dated [●]

#### **ANGLIAN WATER SERVICES FINANCING PLC**

**Issue of [Aggregate Nominal Amount of Tranche] [Title of Bonds] unconditionally and irrevocably guaranteed by, *inter alios*, ANGLIAN WATER SERVICES LIMITED [and unconditionally and irrevocably guaranteed as to scheduled payment of principal and interest pursuant to a financial guarantee insurance policy issued by [MBIA Assurance S.A.]/[other]] under the €10,000,000,000 Global Secured Medium Term Note Programme**

#### **PART A – CONTRACTUAL TERMS**

Terms used herein shall be deemed to be defined as such for the purposes of the conditions set forth in the Prospectus dated 23 September 2005 [and the supplemental Prospectus dated [●]] which [together] constitute[s] a base prospectus for the purposes of the Prospectus Directive (Directive 2003/71/EC) (the “**Prospectus Directive**”). This document constitutes the Final Terms of the Bonds described herein for the purposes of Article 5.4 of the Prospectus Directive and must be read in conjunction with such Prospectus [as so supplemented]. Full information on the Issuer and the offer of the Bonds is only available on the basis of the combination of these Final Terms and the Prospectus. [The Prospectus [and the supplemental Prospectus] [is] [are] available for viewing at Anglian House, Ambury Road, Huntingdon, Cambridgeshire PE29 3NZ [and] [www.anglianwater.co.uk] and copies may be obtained from Anglian House, Ambury Road, Huntingdon, Cambridgeshire PE29 3NZ.]

*[The following alternative language applies if the first tranche of an issue which is being increased was issued under a Prospectus with an earlier date.]*

[Terms used herein shall be deemed to be defined as such for the purposes of the Conditions (the “**Conditions**”) set forth in the Prospectus dated [original date] [and the supplemental Prospectus dated [●]]. This document constitutes the Final Terms of the Bonds described herein for the purposes of Article 5.4 of the Prospectus Directive (Directive 2003/71/EC) (the “**Prospectus Directive**”) and must be read in conjunction with the Prospectus dated [current date] [and the supplemental Prospectus dated [●]], which [together] constitute[s] a base prospectus for the purposes of the Prospectus Directive, save in respect of the Conditions which are extracted from the Prospectus dated [original date] [and the supplemental Prospectus dated [●]] and are attached hereto. Full information on the Issuer and the offer of the Bonds is only available on the basis of the combination of these Final Terms and the Prospectuses dated [original date] and [current date] [and the supplemental Prospectuses dated [●] and [●]]. [The Prospectuses [and the supplemental Prospectuses] are available for viewing at Anglian House, Ambury Road, Huntingdon, Cambridgeshire PE29 3NZ [and] [www.anglianwater.co.uk] and copies may be obtained from Anglian House, Ambury Road, Huntingdon, Cambridgeshire PE29 3NZ.]

[Repayment of the principal and payment of any interest or premium in connection with the Bonds has not been guaranteed by MBIA Assurance S.A. or by any other financial institution.]

*[Note: include above paragraph if not Wrapped Bonds being described in the Final Terms.]*

[Include whichever of the following apply or specify as “Not Applicable” (N/A). Note that the numbering should remain as set out below, even if “Not Applicable” is indicated for individual paragraphs or subparagraphs.]

[If the Bonds must be redeemed before the first anniversary of their date of issue, the minimum denomination must be £100,000 or its equivalent in any other currency.]

[When completing final terms or adding any other final terms or information consideration should be given as to whether such terms or information constitute “significant new factors” and consequently trigger the need for a supplement to the Prospectus under Article 16 of the Prospectus Directive.]

1. (i) Issuer: Anglian Water Services Financing Plc
- (ii) Obligors: Anglian Water Services Limited, Anglian Water Services Holdings Limited and Anglian Water Services Overseas Holdings Limited
- (iii) Financial Guarantor: [MBIA/Specify Other]  
(Delete if not Wrapped Bonds)  
[NB: Supplemental prospectus or new prospectus required prior to issue of Wrapped Bonds]
2. (i) Series Number: [ ]
- (ii) Tranche Number: [ ]
- (iii) [Nature of Bonds: USPP Bonds]
3. Specified Currency or Currencies: [ ]
4. Aggregate Nominal Amount of Bonds admitted to trading:
  - (i) Series: [ ]
  - (ii) Tranche: [ ]
5. Issue Price of Tranche: [ ] per cent. of the Aggregate Nominal Amount [plus accrued interest from [insert date] (in the case of fungible issues only, if applicable)].
  - (iv) Net Proceeds: [ ]  
(Required only for listed issues)
6. Specified Denominations: [ ]  
(in the case of Registered Bonds, this means the minimum integral amount in which transfers can be made)
 

Tradeable Amount: [ ]
7. (i) Issue Date: [ ]
- (ii) Interest Commencement Date: [ ]  
(if different from Issue Date)

8. Maturity Date: *[Fixed rate – specify date/Floating rate – Interest Payment Date falling in or nearest to [specify month and year]*
9. Interest Basis: *[[ ] per cent. Fixed Rate]  
[[LIBOR/EURIBOR] +/- [ ] per cent. Floating Rate]  
[Zero Coupon]  
[Index Linked Interest]  
[Dual Currency Interest]  
[specify other]  
(further particulars specified below)*
10. Redemption/Payment Basis: *[Redemption at par]  
[Index Linked Redemption]  
[Dual Currency Redemption]  
[Partly Paid]  
[Instalment]  
[US Change of Control Redemption Event]  
[specify other]*
11. Change of Interest Basis or Redemption/Payment Basis: *[Specify details of any provision for change of Bonds into another interest basis or redemption/ payment basis]*
12. Call Options: *[Issuer Call]  
[(further particulars specified below)]*
13. (i) Status of the Bonds: *[If Class A Wrapped Bonds or Class A Unwrapped Bonds:]*
- The Class A Wrapped Bonds and the Class A Unwrapped Bonds will rank *pari passu* among each other in terms of interest and principal payments and rank in priority to the Class B Wrapped Bonds and the Class B Unwrapped Bonds.
- [If Class B Wrapped Bonds or Class B Unwrapped Bonds:]*
- The Class B Wrapped Bonds and the Class B Unwrapped Bonds will rank *pari passu* among each other and are subordinated in terms of interest and principal payments to the Class A Wrapped Bonds and the Class A Unwrapped Bonds.
- (ii) Status of the Guarantees: Senior
- (iii) [Status of the Bond Policy: *(Only required if Wrapped Bonds)]*
- The Bond Policy will rank *pari passu* with all other unsecured obligations of the Financial Guarantor]
- (iv) [Financial Guarantor Event of Default (if not MBIA): *(Only required if Wrapped Bonds)  
[Specify for Financial Guarantor]*

- [iii] [Date [Board] approval for issuance of Bonds [and Bond Policy] obtained: [●] and [●] respectively]]  
*(N.B. Only relevant where Board (or similar) authorisation is required for the particular tranche of Bonds or related Bond Policy)*
14. Listing: [London/specify other/specify market/None]
15. Method of distribution: [Syndicated/Non-syndicated]

**PROVISIONS RELATING TO INTEREST (IF ANY) PAYABLE**

16. **Fixed Rate Bond Provisions** [Applicable/Not Applicable]  
*(If not applicable, delete the remaining sub paragraphs of this paragraph)*
- (i) Rate(s) of Interest: [ ] per cent. per annum [payable [annually/semi-annually/quarterly] in arrear] *(If payable other than annually, consider amending Condition 6)*
- (ii) Interest Payment Date(s): [[ ] in each year up to and including the Maturity Date]/[specify other]  
*(NB: This will need to be amended in the case of long or short coupons)*
- (iii) Fixed Coupon Amount(s): [ ] per [ ] in nominal amount
- (iv) Broken Amount(s): *[Insert particulars of any initial or final broken interest amounts which do not correspond with the Fixed Coupon Amount]*
- (v) Day Count Fraction: [30/360 or Actual/Actual (ICMA) or specify other]
- (vi) Determination Date[s]: [ ] in each year  
*[Insert regular interest payment dates, ignoring issue date of maturity date in the case of a long or short first or last coupon.*  
*NB: This will need to be amended in the case of regular interest payment dates which are not of equal duration*  
*NB: Only relevant where Day Count Fraction is Actual/Actual (ICMA)]*
- (vii) Other terms relating to the method of calculating interest for Fixed Rate Bonds: [None/Give details]
17. **Floating Rate Bond Provisions** [Applicable/Not Applicable]  
*(If not applicable, delete the remaining subparagraphs of this paragraph)*
- (i) Specified Period(s)/Specified Interest Payment Dates: [ ]
- (ii) Business Day Convention: [Floating Rate Convention/Following Business Day Convention/Modified Following Business Day Convention/Preceding Business Day Convention/[specify other]]
- (iii) Additional Business Centre(s): [ ]



- (iv) Manner in which the Rate of Interest and Interest Amount is to be determined: [Screen Rate Determination/ISDA Determination/specify other]
- (v) Party responsible for calculating the Rate of Interest and Interest Amount (if not the Principal Paying Agent): [ ]
- (vi) Screen Rate Determination:
- Reference Rate: [ ]  
(Either LIBOR, EURIBOR or other, although additional information is required if other – including fallback provisions)
  - Interest Determination Date(s): [ ]  
(Second London business day prior to the start of each Interest Period if LIBOR (other than Sterling or euro LIBOR), first day of each Interest Period if Sterling LIBOR and the second day on which the TARGET System is open prior to the start of each Interest Period if EURIBOR or euro LIBOR)
  - Relevant Screen Page: [ ]  
(In the case of EURIBOR, if not Telerate Page 248 ensure it is a page which shows a composite rate or amend the fallback provisions appropriately)
- (vii) ISDA Determination:
- Floating Rate Option: [ ]
  - Designated Maturity: [ ]
  - Reset Date: [ ]
- (viii) Margin(s): [+/-] [ ] per cent. per annum
- (ix) Minimum Rate of Interest: [ ] per cent. per annum
- (x) Maximum Rate of Interest: [ ] per cent. per annum
- (xi) Day Count Fraction: [Actual/365  
Actual/365 (Fixed)  
Actual/365 (Sterling)  
Actual/360  
30/360  
30E/360  
Other]  
(See Condition 7 for alternatives)
- (xii) Fall back provisions (including, if applicable, details of Reference Banks), rounding provisions and any other terms relating to the method of calculating interest on Floating Rate Bonds, if different from those set out in the Conditions: [ ]

18. **Zero Coupon Bond Provisions**

[Applicable/Not Applicable]

*(If not applicable, delete the remaining subparagraphs of this paragraph)*

- (i) Accrual Yield: [ ] per cent. per annum
- (ii) Reference Price: [ ]
- (iii) Any other formula/basis of determining amount payable: [ ]
- (Consider applicable day count fraction if not U.S. dollar denominated)*
- (iv) Day Count Fraction in relation to Early Redemption Amounts and late payment: [Conditions 10(e)(ii) and 10(k) apply/specify other]
- (Consider applicable day count fraction if not U.S. dollar denominated)*
19. **Index Linked Interest/Redemption Bond Provisions** [Applicable/Not Applicable]
- (If applicable, specify which or both of Index Linked Interest Bond or Index Linked Redemption Bond provisions applicable or if not applicable, delete the remaining subparagraphs of this paragraph)*
- (i) Index/Formula: *[give or annex details]*
- (ii) Calculation Agent responsible for calculating the principal and/or interest due: [ ]
- (iii) Provisions for determining coupon where calculation by reference to Index and/or Formula is impossible or impracticable: [ ]
- (iv) Specified Period(s)/Specified Interest Payment Dates: [ ]
- (v) Business Day Convention: [Floating Rate Convention/Following Business Day Convention/Modified Following Business Day Convention/Preceding Business Day Convention/specify other]
- (vi) Additional Business Centre(s): [ ]
- (vii) Minimum Rate of Interest: [ ] per cent. per annum
- (viii) Maximum Rate of Interest: [ ] per cent. per annum
- (ix) Day Count Fraction: [ ]
20. **Indexation Bond Provisions** [Applicable/Not Applicable]
- (If not applicable, delete the remaining subparagraphs of this paragraph)*
- (i) Base Index Figure: [ ]
- (ii) Any other terms relating to indexation, if different from those set out in the Conditions: [ ]
- (iii) Reference Gilt: [ ]

21. **Dual Currency Bond Provisions** [Applicable/Not Applicable]  
*(If not applicable, delete the remaining subparagraphs of this paragraph)*
- (i) Rate of Exchange/method of calculating Rate of Exchange: [give details]
- (ii) Calculation Agent, if any, responsible for calculating the principal and/or interest payable: [ ]
- (iii) Provisions applicable where calculation by reference to Rate of Exchange impossible or impracticable: [ ]
- (iv) Person at whose option Specified Currency(ies) is/are payable: [ ]

**PROVISIONS RELATING TO REDEMPTION**

22. **Issuer Call:** [Applicable/Not Applicable]  
*(If not applicable, delete the remaining subparagraphs of this paragraph)*
- (i) Optional Redemption Date(s): [ ]
- (ii) Optional Redemption Amount of each Bond and method, if any, of calculation of such amount(s): [Spens Price/Par/specify other]  
*(if Spens Price, specify Reference Gilt)*
- (iii) If redeemable in part:
- (a) Minimum Redemption Amount: [ ]
- (b) Maximum Redemption Amount: [ ]
- (iv) Notice period (if other than as set out in the Conditions): [ ]
23. Final Redemption Amount of each Bond: [Par/specify other/see Appendix]
24. Early Redemption Amount of each Bond payable on redemption for taxation reasons or on event of default and/or the method of calculating the same (if required or if different from that set out in Condition 10(e)): [Par/specify other]

**GENERAL PROVISIONS APPLICABLE TO THE BONDS**

25. Form of Bonds: [Bearer Bonds:
- [Temporary Bearer Global Bond exchangeable for a Permanent Bearer Global Bond on or after Exchange Date which is exchangeable for Definitive Bonds [on 60 days' notice given at any time/only upon an Exchange Event].]
- [Temporary Bearer Global Bond exchangeable for Definitive Bonds on and after the Exchange Date.]
- [Permanent Bearer Global Bond exchangeable for Definitive Bonds [on 60 days' notice given at any time/only upon an Exchange Event].]

- [Registered Bonds:
- [Regulation S Global Bond (U.S.\$[ ] nominal amount) registered in the name of a nominee for [DTC/ a common depository for Euroclear and Clearstream, Luxembourg].]
- [Rule 144A Global Bond (U.S.\$[ ] nominal amount registered in the name of a nominee for [DTC/ a common depository for Euroclear and Clearstream, Luxembourg].]
- [Definitive IAI Registered Bonds (*specify nominal amounts*).]
26. Additional Financial Centre(s) or other special provisions relating to Payment Dates: [Not Applicable/*give details*]  
(*Note that this item relates to the place of payment and not Interest Period end dates to which items 17(iii) and 19(vi) relate*)
27. Talons for future Coupons or Receipts to be attached to Definitive Bearer Bonds (and dates on which such Talons mature): [Yes/No. *If yes, give details*]
28. Details relating to Partly Paid Bonds: amount of each payment comprising the Issue Price and date on which each payment is to be made and consequences of failure to pay, including any right of the Issuer to forfeit the Bonds and interest due on late payment: [Not applicable/*give details. NB: new forms of Global Bond may be required for Partly Paid issues.*]
29. Details relating to Instalment Bonds:
- (i) Instalment Amount(s): [Not Applicable/*give details*]
- (ii) Instalment Date(s): [Not Applicable/*give details*]
30. Redenomination applicable: Redenomination [not] applicable  
  
(*If Redenomination is applicable, specify the terms of Redenomination in an Annex to the Final Terms*)
31. Other final terms: [Not Applicable/*give details*]  
  
(*When adding any other final terms consideration should be given as to whether such terms constitute a “significant new factor” and consequently trigger the need for a supplement to the Prospectus under Article 16 of the Prospectus Directive.*)

## DISTRIBUTION

32. (i) If syndicated, names of Managers: [Not Applicable/*give names*]
- (ii) Stabilising Manager (if any): [Not Applicable/*give names*]
33. If non-syndicated, name of relevant Dealer: [ ]
35. Additional selling restrictions: [Not Applicable/*give details*]

**[LISTING AND ADMISSION TO TRADING APPLICATION**

These Final Terms comprise the final terms required to list and have admitted to trading the issue of Bonds described herein pursuant to the listing of the €10,000,000,000 Global Secured Medium Term Note Programme of Anglian Water Services Financing Plc.]

**RESPONSIBILITY**

Each of the Obligors accepts responsibility for the information contained in these Final Terms [save for the [Financial Guarantor] Information]\*.

[The Financial Guarantor accepts responsibility for the [Financial Guarantor] Information contained in this Final Terms.]\*

Each of the Obligors [and the Financial Guarantor] confirms that such information has been accurately reproduced and that, so far as it is aware, and is able to ascertain from information published by [●], no facts have been omitted which would render the reproduced inaccurate or misleading.]

Signed on behalf of the Issuer:

By: .....  
*Duly authorised*

Signed on behalf of Anglian Water Services Limited:

By: .....  
*Duly authorised*

Signed on behalf of Anglian Water Services Holdings Limited:

By: .....  
*Duly authorised*

Signed on behalf of Anglian Water Services Overseas Holdings Limited:

By: .....  
*Duly authorised*

[Signed on behalf of [Financial Guarantor]:

By: .....  
*Duly authorised]\**

If the applicable Final Terms specify any modification to the Terms and Conditions of the Bonds as described herein, it is envisaged that, to the extent that such modification relates only to Conditions 1, 6, 7, 8, 9, 10 (except Condition 10(c)), 15, 16, 17, 18 (insofar as such Bonds are not listed or admitted to trade on any stock exchange) or 22, they will not necessitate the preparation of a supplementary prospectus. If the Terms and Conditions of the Bonds of any Series are to be modified in any other respect, a supplementary prospectus will be prepared, if appropriate.

\* Delete if not applicable

## PART B – OTHER INFORMATION

### 1 Listing

- (i) Listing [London/Luxembourg/other (*specify*)/None]
- (ii) Admission to trading: [Application has been made for the Bonds to be admitted to trading on [●] with effect from [●].] ]Not Applicable.]
- (iii) Estimate of total expenses related to admission to trading: [●]

### 2 Ratings

- (i) Ratings: The Bonds to be issued have been rated:
- [S&P: [●]]
- [Moody's: [●]]
- [[Other]: [●]]

*(The above disclosure should reflect the rating allocated to Bonds of the type being issued under the Programme generally or, where the issue has been specifically rated, that rating.)*

### 3 [Notification

The UK Listing Authority [has been requested to provide/has provided – *include first alternative for an issue which is contemporaneous with the establishment or update of the Programme and the second alternative for subsequent issues*] the [*include names of competent authorities of host Member States*] with a certificate of approval attesting that the Prospectus has been drawn up in accordance with the Prospectus Directive.]

### 4 [Reasons for the offer, estimated net proceeds and total expenses

- (i) [Reasons for the offer: [●]
- (See [“Use of Proceeds” wording in Prospectus – if reasons for offer different from making profit and/or hedging certain risks will need to include those reasons here.)]*
- (ii) [Estimated net proceeds: [●]
- (If proceeds are intended for more than one use will need to split out and present in order of priority. If proceeds insufficient to fund all proposed uses state amount and sources of other funding)]*
- (iii) [Estimated total expenses: [●] (*Include breakdown of expenses.*)
- (Only necessary to include disclosure of net proceeds and total expenses at (ii) and (iii) above where disclosure is included at (i) above).]]<sup>1</sup>*

**5 [Fixed Rate Bonds only – YIELD]**

Indication of yield: [●]

The yield is calculated at the Issue Date on the basis of the Issue Price. It is not an indication of future yield.]

**6 [Index-Linked or other variable-linked Bonds only – PERFORMANCE OF INDEX/FORMULA/ OTHER VARIABLE AND OTHER INFORMATION CONCERNING THE UNDERLYING]**

*Need to include details of where past and future performance and volatility of the index/formula/other variable can be obtained. Where the underlying is an index need to include the name of the index and a description if composed by the Issuer and if the index is not composed by the Issuer need to include details of where the information about the index can be obtained. Where the underlying is not an index need to include equivalent information.]<sup>2</sup>*

**7 [Dual currency Bonds only – PERFORMANCE OF RATE[S] OF EXCHANGE]**

*Need to include details of where past and future performance and volatility of the relevant rate[s] can be obtained.]<sup>3</sup>*

**8 Operational information**

ISIN Code: [●]

Common Code: [●]

Any clearing system(s) other than Euroclear Bank S.A./N.V. and Clearstream Banking Société Anonyme and the relevant identification number(s): [Not Applicable/give name(s) and member(s) [and address(es)]]

Delivery: Delivery [against free of] payment

Names and addresses of additional Paying Agent(s) (if any): [●]

**9 General**

Applicable TEFRA exemption: [C Rules/D Rules/Not Applicable]

Notes:

- (1) Required for derivative securities
- (2) Required for derivative securities
- (3) Required for derivative securities

## CHAPTER 9

### TERMS AND CONDITIONS OF THE BONDS

*The following (other than the italicised portions) are the Terms and Conditions of the Bonds which will be incorporated by reference into each Global Bond (as defined below) and each definitive Bond, in the latter case only if permitted by the relevant stock exchange (if any) and agreed by the Issuer and the relevant Dealer at the time of issue but, if not so permitted and agreed, such definitive Bond will have endorsed thereon or attached thereto such Terms and Conditions. The applicable Final Terms in relation to any Tranche of Bonds may specify other terms and conditions which shall, to the extent so specified or to the extent inconsistent with the following Terms and Conditions, replace or modify the following Terms and Conditions for the purpose of such Bonds. The applicable Final Terms (or the relevant provisions thereof) will be endorsed upon, or attached to, each Global Bond and definitive Bond. Reference should be made to “Form of the Bonds” for a description of the content of Final Terms which will specify which of such terms are to apply in relation to the relevant Bonds.*

This Bond is one of a Series (as defined below) of Bonds issued by Anglian Water Services Financing Plc (the “**Issuer**”) constituted by a trust deed dated 30 July 2002 between the Issuer, Anglian Water Services Limited (“**AWS**”), Anglian Water Services Holdings Limited (“**AWS Holdings**”), Anglian Water Services Overseas Holdings Limited (“**AWS Overseas Holdings**”), MBIA Assurance S.A. (“**MBIA**”) and Deutsche Trustee Company Limited as trustee (the “**Bond Trustee**”, which expression includes the trustee or trustees for the time being of the Bond Trust Deed) (such trust deed as modified and restated by a first supplemental trust deed dated on or about 23 September 2005 and as further modified and/or supplemented and/or restated from time to time, the “**Bond Trust Deed**”).

The payment of all amounts in respect of the Bonds has been secured by the Issuer and guaranteed and secured by each of AWS, AWS Holdings and AWS Overseas Holdings (each, together with the Issuer, an “**Obligor**” and together, the “**AWS Financing Group**”) in the Security Agreement (as defined below).

In addition, the Class A Wrapped Bonds and the Class B Wrapped Bonds (each as defined in Condition 1(a) below) only shall be unconditionally and irrevocably guaranteed as to scheduled payments of principal and interest (as adjusted for indexation but excluding certain amounts including any additional amounts relating to prepayment or any accelerated amounts or amounts by which the Rate of Interest exceeds the initial Rate of Interest applicable to such Series as at the relevant Issue Date (together, the “**FG Excepted Amounts**”) in respect of such Class A Wrapped Bonds and Class B Wrapped Bonds pursuant to a financial guarantee insurance policy (each a “**Bond Policy**”) to be issued by MBIA or another financial guarantor (each a “**Financial Guarantor**”) in conjunction with the issue of Class A Wrapped Bonds and Class B Wrapped Bonds.

None of the Class A Unwrapped Bonds or Class B Unwrapped Bonds (each as defined in Condition 1(a) below) will have the benefit of any such Bond Policy.

References herein to the “**Bonds**” shall be references to the Bonds of this Series and of each Class and shall mean:

- (i) in relation to any Bonds represented by a global Bond (a “**Global Bond**”), units of the lowest Specified Denomination (as specified in the applicable Final Terms) in the Specified Currency;
- (ii) any Global Bond;
- (iii) any definitive Bonds in bearer form (“**Bearer Bonds**”) issued in exchange for a Global Bond in bearer form; and
- (iv) definitive Bonds in registered form (“**Registered Bonds**”) (whether or not issued in exchange for a Global Bond in registered form).

The Bonds, the Receipts (as defined below) and the Coupons (as defined below) have the benefit of an agency agreement dated 30 July 2002 (such agency agreement as supplemented on or about 23 September 2005 and as further amended and/or supplemented and/or restated from time to time, the “**Agency Agreement**”) and made between the Issuer and the other Obligors, the Bond Trustee, Deutsche Bank AG, London as issuing and principal paying agent and agent bank (the “**Principal Paying Agent**”, which expression shall include any successor principal paying agent and agent bank) and any other paying agents appointed from time to time under the Agency Agreement (together with the Principal Paying Agent, the “**Paying Agents**”, which expression shall include any successor paying agents), Deutsche Bank Trust Company Americas as exchange agent (the



“**Exchange Agent**” which expression shall include any successor exchange agent) and as registrar (the “**Registrar**”, which expression shall include any successor registrar) and Deutsche Bank AG, London Branch as a transfer agent (together with the Registrar, the “**Transfer Agents**”, which expression shall include any additional or successor transfer agents).

Interest bearing definitive Bearer Bonds have interest coupons (“**Coupons**”) and, if indicated in the applicable Final Terms, talons for further Coupons (“**Talons**”) attached on issue. Any reference herein to Coupons or coupons shall, unless the context otherwise requires, be deemed to include a reference to Talons or talons. Definitive Bearer Bonds repayable in instalments have receipts (“**Receipts**”) for the payment of the instalments of principal (other than the final instalment) attached on issue. Registered Bonds and Global Bonds do not have Receipts, Coupons or Talons attached on issue.

The Final Terms for this Bond (or the relevant provisions thereof) are attached to or endorsed on this Bond and supplements these Terms and Conditions and may specify other terms and conditions which shall, to the extent so specified or to the extent inconsistent with these Terms and Conditions, replace or modify these Terms and Conditions for the purposes of this Bond. References to the “**applicable Final Terms**” are to the Final Terms (or the relevant provisions thereof) attached to or endorsed on this Bond.

Any reference to “**Bondholders**” or “**holders**” in relation to any Bonds shall mean (in the case of Bearer Bonds) the holders of the Bonds and (in the case of Registered Bonds) the persons in whose name the Bonds are registered and shall, in relation to any Bonds represented by a global Bond, be construed as provided below. Any reference herein to “**Receiptholders**” shall mean the holders of the Receipts and any reference herein to “**Couponholders**” shall mean the holders of the Coupons and shall, unless the context otherwise requires, include the holders of the Talons.

As used herein, “**Tranche**” means Bonds which are identical in all respects (including as to listing) and “**Series**” means a Tranche of Bonds together with any further Tranche or Tranches of Bonds which are (i) expressed to be consolidated and form a single series and (ii) identical in all respects (including as to listing) except for their respective Issue Dates, Interest Commencement Dates and/or Issue Prices.

Each Obligor has, on 30 July 2002, entered into the security agreement (the “**Security Agreement**”) with Deutsche Trustee Company Limited as security trustee (the “**Security Trustee**”), pursuant to which each Obligor guarantees the obligations of each other Obligor under the Finance Documents (as defined below) to the Security Trustee as security trustee for the Secured Creditors (as defined below) and grants certain fixed and floating charge security (the “**Security**”) to the Security Trustee for itself and on behalf of the Bond Trustee (for itself and on behalf of the Bondholders), the Bondholders, the USPP 2001 Bondholders, the Initial Financial Guarantor, the Existing Finance Lessors, the Existing Hedge Counterparties, the Issuer, the Initial Authorised Credit Facility Agent, the Initial Authorised Credit Facility Arrangers, the Original Lenders, the O&M Facility Reserve Provider, the Debt Service Reserve Liquidity Providers, the Account Bank, the Cash Manager, the Agent Bank, the Principal Paying Agent, the Registrar, the Exchange Agent and the Transfer Agents (each as defined in the Master Definitions Agreement (as defined below)) together with any receiver and any additional creditor of the AWS Financing Group which accedes to the STID (as defined below) and the Common Terms Agreement (as defined below) (together, the “**Secured Creditors**”).

The Obligors have also entered into a security and trust intercreditor deed dated 30 July 2002 (the “**STID**”) with, *inter alios*, the Security Trustee and the other Secured Creditors pursuant to which the Security Trustee holds the Security on trust for the Secured Creditors and the Secured Creditors agree to certain intercreditor arrangements.

The Issuer has entered or may enter into liquidity facility agreements (together, the “**Liquidity Facility Agreements**”) with certain liquidity facility providers (together, “**Liquidity Facility Providers**”), pursuant to which the Liquidity Facility Providers agree to make certain facilities available to meet debt service liquidity shortfalls and shortfalls in projected operating and maintenance expenditure of the AWS Financing Group.

The Issuer has entered or may enter into a bank lending facility or an authorised loan agreement (the “**Authorised Loan Agreement**”) with, *inter alios*, certain lenders who agree to make certain facilities available to the Issuer for the purposes of funding certain working capital, capital expenditure and other expenses.

The Issuer has entered or may enter into certain currency and interest-rate hedging agreements and other derivative transactions (together, the “**Hedging Agreements**”) with certain hedge counterparties (together, the

“**Hedge Counterparties**”), pursuant to which the Issuer hedges certain of its currency and interest-rate obligations.

The Obligors have entered into a common terms agreement dated 30 July 2002 (the “**Common Terms Agreement**”) with, *inter alios*, the Security Trustee and the other Secured Creditors, which contains certain representations and covenants of the Issuer and the other Obligors and events of default relating to, *inter alia*, the Bonds.

The Issuer has entered into intercompany loan arrangements (the “**Intercompany Loan Arrangements**”) under which the Issuer agreed to make available loan facilities and other financial accommodation to AWS.

The Bond Trust Deed, the Bonds, the Bond Policy, the Common Terms Agreement, the Security Agreement, the STID, the Agency Agreement, the Liquidity Facility Agreements, the Hedging Agreements, the Issuer/AWS Loan Agreement, the AWS Loan Notes, the Bridging Facility Agreement, the Authorised Loan Agreement, the I&I Agreements and the Master Definitions Agreement dated 30 July 2002 (the “**Master Definitions Agreement**”) and, together with the other documents referred to in the Master Definitions Agreement, the “**Finance Documents**”.

Copies of, *inter alia*, the Bond Trust Deed, the Common Terms Agreement, the Security Agreement, the STID, the Agency Agreement, the Liquidity Facility Agreements, the Hedging Agreements, the Bridging Facility Agreement, the Authorised Loan Agreement, the I&I Agreements and the Master Definitions Agreement are available for inspection during normal business hours at the specified office of each of the Principal Paying Agent, the Registrar and any other Paying Agents and Transfer Agents (such Paying Agents and the Transfer Agents being together referred to as the “**Agents**”). Copies of the applicable Final Terms are obtainable during normal business hours at the specified office of each of the Agents save that, if this Bond is an unlisted Bond of any Series, the applicable Final Terms will only be obtainable by a Bondholder holding one or more unlisted Bonds of that Series and such Bondholder must produce evidence satisfactory to the Issuer and the relevant Agent as to its holding of such Bonds and identity.

The Bondholders, the Receiptholders and the Couponholders are deemed to have notice of, and are entitled to the benefit of, all the provisions of the Bond Trust Deed, the Common Terms Agreement, the Security Agreement, the STID and the applicable Final Terms and to have notice of those provisions of the Agency Agreement and the other Finance Documents which are applicable to them. The statements in these Terms and Conditions include summaries of, and are subject to, the detailed provisions of the Agency Agreement, the Bond Trust Deed, the Security Agreement, the Common Terms Agreement and the STID.

Words and expressions defined in the Bond Trust Deed and/or the Agency Agreement and/or the Master Definitions Agreement or used in the applicable Final Terms shall have the same meanings where used in these Terms and Conditions unless the context otherwise requires or unless otherwise stated and provided that, in the event of inconsistency between the Master Definitions Agreement and the applicable Final Terms, the applicable Final Terms will prevail.

Any reference in these Conditions to a matter being “specified” means as the same may be specified in the applicable Final Terms.

## **1. CLASSES, FORM, DENOMINATION AND TITLE**

### **(a) Classes of Bonds**

Each Series of Bonds belongs to one of four classes of Bonds (each a “**Class**”). The available Classes of Bonds will be “**Class A Wrapped Bonds**”, “**Class A Unwrapped Bonds**”, “**Class B Wrapped Bonds**” and “**Class B Unwrapped Bonds**”.

### **(b) Form and Denomination**

The Bonds are in bearer form or in registered form as specified in the applicable Final Terms and, in the case of definitive Bonds, serially numbered, in the Specified Currency and the Specified Denomination(s) provided that in the case of any Bonds which are to be admitted to trading on a regulated market within the European Economic Area or offered to the public in a Member State of the European Economic Area in circumstances which require the publication of a prospectus under the Prospectus Directive, the minimum Specified Denomination shall be €50,000 (or its equivalent in any other currency as at the date of issue of the relevant Bonds). Bonds of one Specified Denomination may not be exchanged for Bonds of

another Specified Denomination and Bearer Bonds may not be exchanged for Registered Bonds and vice versa.

*So long as the Bonds are represented by a temporary Global Bond or permanent Global Bond and the relevant clearing system(s) so permit, the Bonds shall be tradeable only in principal amounts of at least the Specified Denomination (or if more than one Specified Denomination, the lowest Specified Denomination) provided hereon and integral multiples of the Tradeable Amount provided in the relevant Final Terms.*

This Bond may be a Fixed Rate Bond, an Indexation Bond, a Floating Rate Bond, a Zero Coupon Bond, an Index Linked Interest Bond, a Dual Currency Interest Bond or a combination of any of the foregoing, depending upon the Interest Basis shown in the applicable Final Terms.

This Bond may be an Index Linked Redemption Bond, an Instalment Bond, a Dual Currency Redemption Bond, a Partly Paid Bond or a combination of any of the foregoing, depending upon the Redemption/Payment Basis shown in the applicable Final Terms.

Definitive Bearer Bonds are issued with Coupons attached, unless they are Zero Coupon Bonds in which case references to Coupons and Couponholders in these Terms and Conditions are not applicable.

**(c) Title**

Subject as set out below, title to the Bearer Bonds, Receipts and Coupons will pass by delivery and title to the Registered Bonds will pass upon registration of transfers in accordance with the provisions of the Agency Agreement. The Issuer and each of the other Obligors, the Bond Trustee and any Agent will (except as otherwise required by law) deem and treat the bearer of any Bearer Bond, Receipt or Coupon and the registered holder of any Registered Bond as the absolute owner thereof (whether or not overdue and notwithstanding any notice of ownership or writing thereon or notice of any previous loss or theft thereof) for all purposes but, in the case of any Global Bond, without prejudice to the provisions set out in the next succeeding paragraph and no person will be liable for treating such holder.

For so long as any of the Bonds are represented by a Global Bond held on behalf of Euroclear Bank S.A./N.V. as operator of the Euroclear System (“**Euroclear**”) and/or Clearstream Banking, société anonyme (“**Clearstream, Luxembourg**”), each person (other than Euroclear or Clearstream, Luxembourg) who is for the time being shown in the records of Euroclear or of Clearstream, Luxembourg as the holder of a particular nominal amount of such Bonds (in which regard any certificate or other document issued by Euroclear or Clearstream, Luxembourg as to the nominal amount of such Bonds standing to the account of any person shall be conclusive and binding for all purposes save in the case of manifest error) shall be treated by the Issuer, the Obligors, the Security Trustee, the Bond Trustee and the Agents as the holder of such nominal amount of such Bonds for all purposes other than with respect to the payment of principal or interest on such nominal amount of such Bonds, for which purpose the bearer of the relevant Bearer Global Bond or the registered holder of the relevant Registered Global Bond shall be treated by the Issuer, the Obligors, the Security Trustee, the Bond Trustee and any Agent as the holder of such nominal amount of such Bonds in accordance with and subject to the terms of the relevant Global Bond and the expressions “**Bondholder**” and “**holder of Bonds**” and related expressions shall be construed accordingly.

For so long as The Depository Trust Company (“**DTC**”) or its nominee is the registered owner or holder of a Registered Global Bond, DTC or such nominee, as the case may be, will be considered the sole owner or holder of the Bonds represented by such Registered Global Bond for all purposes under the STID, the Bond Trust Deed, the Agency Agreement and the Bonds except to the extent that in accordance with DTC’s published rules and procedures any ownership rights may be exercised by its participants or beneficial owners through participants.

Bonds which are represented by a Global Bond will be transferable only in accordance with the rules and procedures for the time being of DTC, Euroclear and Clearstream, Luxembourg, as the case may be. References to DTC, Euroclear and/or Clearstream, Luxembourg shall, whenever the context so permits, be deemed to include a reference to any additional or alternative clearing system specified in the applicable Final Terms or as may otherwise be approved by the Issuer, the Principal Paying Agent and the Bond Trustee.

## 2. TRANSFERS OF REGISTERED BONDS

### (a) Transfers of interests in Registered Global Bonds

Transfers of beneficial interests in Registered Global Bonds will be effected by DTC, Euroclear or Clearstream, Luxembourg, as the case may be, and, in turn, by other participants and, if appropriate, indirect participants in such clearing systems acting on behalf of beneficial transferors and transferees of such interests. A beneficial interest in a Registered Global Bond will, subject to compliance with all applicable legal and regulatory restrictions, be transferable for Bonds in definitive form or for a beneficial interest in another Registered Global Bond only in the authorised denominations set out in the applicable Final Terms and only in accordance with the rules and operating procedures for the time being of DTC, Euroclear or Clearstream, Luxembourg, as the case may be, and in accordance with the terms and conditions specified in the Agency Agreement. Transfers of a Registered Global Bond registered in the name of a nominee for DTC shall be limited to transfers of such Registered Global Bond, in whole but not in part, to another nominee of DTC or to a successor of DTC or such successor's nominee.

### (b) Transfers of Registered Bonds in definitive form

Subject as provided in paragraph (g) below, upon the terms and subject to the conditions set forth in the Agency Agreement, a Registered Bond in definitive form may be transferred in whole or in part (in the authorised denominations set out in the applicable Final Terms). In order to effect any such transfer (i) the holder or holders must (A) surrender the Registered Bond for registration of the transfer of the Registered Bond (or the relevant part of the Registered Bond) at the specified office of the Registrar or any Transfer Agent, with the form of transfer thereon duly executed by the holder or holders thereof or his or their attorney or attorneys duly authorised in writing and (B) complete and deposit such other certifications as may be required by the Registrar or, as the case may be, the relevant Transfer Agent and (ii) the Registrar or, as the case may be, the relevant Transfer Agent must, after due and careful enquiry, be satisfied with the documents of title and the identity of the person making the request. Any such transfer will be subject to such reasonable regulations as the Issuer and the Registrar may from time to time prescribe (the initial such regulations being set out in Schedule 5 to the Agency Agreement). Subject as provided above, the Registrar or, as the case may be, the relevant Transfer Agent will, within three business days (being for this purpose a day on which banks are open for business in the city where the specified office of the Registrar or, as the case may be, the relevant Transfer Agent is located) of the request (or such longer period as may be required to comply with any applicable fiscal or other laws or regulations), authenticate and deliver, or procure the authentication and delivery of, at its specified office to the transferee or (at the risk of the transferee) send by uninsured mail, to such address as the transferee may request, a new Registered Bond in definitive form of a like aggregate nominal amount to the Registered Bond (or the relevant part of the Registered Bond) transferred. In the case of the transfer of part only of a Registered Bond in definitive form, a new Registered Bond in definitive form in respect of the balance of the Registered Bond not transferred will be so authenticated and delivered or (at the risk of the transferor) sent to the transferor.

Transfers of Registered Bonds in definitive form may also be made:

- (i) to a transferee who takes delivery also through an interest in a Regulation S Global Bond, upon receipt by the Registrar of a written confirmation substantially in the form set out in the Agency Agreement, amended as appropriate (a “**Transfer Certificate**”) from the transferor to the effect that such transfer is being made in accordance with Regulation S and that, if such transfer is being made prior to expiry of the applicable Distribution Compliance Period, the interests in the Bonds being transferred will be held immediately thereafter through Euroclear and/or Clearstream, Luxembourg; or
- (ii) to a transferee who takes delivery of such interest through a Legended Bond:
  - (A) where the transferee is a person whom the transferor reasonably believes is a QIB in a transaction meeting the requirements of Rule 144A, without certification; or
  - (B) where the transferee is an Institutional Accredited Investor, subject to delivery to the Registrar of a Transfer Certificate from the transferor to the effect that such transfer is being made to an Institutional Accredited Investor, together with a duly executed IAI Investment Letter from the relevant transferee; or

- (iii) otherwise pursuant to the Securities Act or an exemption therefrom, subject to receipt by the Issuer of such satisfactory evidence as the Issuer may reasonably require, which may include an opinion of U.S. counsel, that such transfer is in compliance with any applicable securities laws of any State of the United States,

and, in each case, in accordance with any applicable securities laws of any State of the United States or any other jurisdiction.

Registered Bonds in definitive form transferred by Institutional Accredited Investors to QIBs pursuant to Rule 144A or outside the United States pursuant to Regulation S will be eligible to be held by such QIBs or non-U.S. investors through DTC, Euroclear or Clearstream, Luxembourg, as appropriate, and the Registrar will arrange for any Bonds which are the subject of such a transfer to be represented by the appropriate Registered Global Bond, where applicable.

Upon the transfer, exchange or replacement of Registered Bonds in definitive form, or upon specific request for removal of the Legend on such Bond, the Registrar shall deliver only Registered Bonds in definitive form or refuse to remove the Legend, as the case may be, unless there is delivered to the Issuer such satisfactory evidence as may reasonably be required by the Issuer, which may include an opinion of U.S. counsel, that neither the Legend nor the restrictions on transfer set forth therein are required to ensure compliance with the provisions of the Securities Act.

**(c) Registration of transfer upon partial redemption**

In the event of a partial redemption of Bonds under Condition 10, the Issuer shall not be required to register the transfer of any Registered Bond, or part of a Registered Bond, called for partial redemption.

**(d) Costs of registration**

Bondholders will not be required to bear the costs and expenses of effecting any registration of transfer as provided above, except for any costs or expenses of delivery other than by regular uninsured mail and except that the Issuer may require the payment of a sum sufficient to cover any stamp duty, tax or other governmental charge that may be imposed in relation to the registration.

**(e) Transfers of interests in Regulation S Global Bonds**

Prior to expiry of the applicable Distribution Compliance Period, transfers by the holder of, or of a beneficial interest in, a Regulation S Global Bond to a transferee in the United States or who is a U.S. person will only be made (i) upon receipt by the Registrar of a Transfer Certificate, copies of which are available from the specified office of the Registrar or any Transfer Agent, from the transferor of the Bond or beneficial interest therein to the effect that such transfer is being made to a person whom the transferor reasonably believes is a QIB in a transaction meeting the requirements of Rule 144A; or (ii) otherwise pursuant to the Securities Act or an exemption therefrom, subject to receipt by the Issuer of such satisfactory evidence as the Issuer may reasonably require, which may include an opinion of U.S. counsel, that such transfer is in compliance with any applicable securities laws of any State of the United States, and, in each case, in accordance with any applicable securities laws of any State of the United States or any other jurisdiction.

In the case of (i) above, such transferee may take delivery through a Legended Bond in global or definitive form. After expiry of the applicable Distribution Compliance Period (i) beneficial interests in Regulation S Global Bonds registered in the name of a nominee for DTC may be held through DTC directly, by a participant in DTC, or indirectly through a participant in DTC and (ii) such certification requirements will no longer apply to such transfers.

**(f) Transfers of interests in Rule 144A Global Bonds**

Transfers of Rule 144A Global Bonds or beneficial interests therein may be made:

- (i) to a transferee who takes delivery of such interest through a Regulation S Global Bond, upon receipt by the Registrar of a duly completed Transfer Certificate from the transferor to the effect that such transfer is being made in accordance with Regulation S and that, in the case of a Regulation S Global Bond registered in the name of a nominee for DTC, if such transfer is being made prior to expiry of the applicable Distribution Compliance Period, the interests in the Bonds

being transferred will be held immediately thereafter through Euroclear and/or Clearstream, Luxembourg; or

- (ii) to a transferee who takes delivery of such interest through a Rule 144A Global Bond where the transferee is a person whom the transferor reasonably believes is a QIB in a transaction meeting the requirements of Rule 144A, without certification; or
- (iii) otherwise pursuant to the Securities Act or an exemption therefrom, subject to receipt by the Issuer of such satisfactory evidence as the Issuer may reasonably require, which may include an opinion of U.S. counsel, that such transfer is in compliance with any applicable securities laws of any State of the United States,

and, in each case, in accordance with any applicable securities laws of any State of the United States or any other jurisdiction.

Upon the transfer, exchange or replacement of Rule 144A Global Bonds, or upon specific request for removal of the Legend on such Bond, the Registrar shall deliver only Rule 144A Global Bonds or refuse to remove the Legend, as the case may be, unless there is delivered to the Issuer such satisfactory evidence as may reasonably be required by the Issuer, which may include an opinion of U.S. counsel, that neither the Legend nor the restrictions on transfer set forth therein are required to ensure compliance with the provisions of the Securities Act.

**(g) Exchanges and transfers of Registered Bonds generally**

Holder of Registered Bonds in definitive form, other than Institutional Accredited Investors, may exchange such Bonds for interests in a Registered Global Bond of the same type at any time.

**(h) Definitions**

In this Condition, the following expressions shall have the following meanings:

“**Distribution Compliance Period**” means the period that ends 40 days after the completion of the distribution of each Tranche of Bonds, as certified by the relevant Dealer (in the case of a non-syndicated issue) or the relevant Lead Manager (in the case of a syndicated issue);

“**IAI Investment Letter**” means a letter from an Institutional Accredited Investor in or substantially in the form set out in the Agency Agreement;

“**Institutional Accredited Investor**” means “accredited investors” (as defined in Rule 501(a)(1), (2), (3) or (7) under the Securities Act) that are institutions;

“**Legended Bond**” means Registered Bonds in definitive form that are issued to Institutional Accredited Investors and Registered Bonds (whether in definitive form or represented by a Registered Global Bond) sold in transactions to QIBs in accordance with the requirements of Rule 144A;

“**QIB**” means a “**qualified institutional buyer**” within the meaning of Rule 144A;

“**Regulation S**” means Regulation S under the Securities Act;

“**Regulation S Global Bond**” means a Registered Global Bond representing Bonds sold outside the United States in reliance on Regulation S;

“**Rule 144A**” means Rule 144A under the Securities Act;

“**Rule 144A Global Bond**” means a Registered Global Bond representing Bonds sold in the United States or to QIBs; and

“**Securities Act**” means the United States Securities Act of 1933, as amended.

**3. STATUS OF THE BONDS, GUARANTEES AND BOND POLICY**

**(a) Status of Class A Wrapped Bonds and Class A Unwrapped Bonds**

*This Condition 3(a) is applicable only in relation to Bonds which are specified as being Class A Wrapped Bonds or Class A Unwrapped Bonds.*

The Bonds and any relative Receipts and Coupons are direct and unconditional, obligations of the Issuer, are secured in the manner described in Condition 4 and rank *pari passu* without any preference among themselves. However, the Class A Unwrapped Bonds will not have the benefit of any Bond Policy.

**(b) Status of Class B Wrapped Bonds and Class B Unwrapped Bonds**

*This Condition 3(b) is applicable only in relation to Bonds which are specified as being Class B Wrapped Bonds or Class B Unwrapped Bonds.*

The Bonds and any relative Receipts and Coupons are direct and unconditional obligations of the Issuer, are secured in the manner described in Condition 4, are subordinated to the Class A Wrapped Bonds and the Class A Unwrapped Bonds and rank *pari passu* without any preference among themselves. However, the Class B Unwrapped Bonds will not have the benefit of any Bond Policy.

**(c) Guarantees by the Obligors**

The obligations of the Obligors under the Finance Documents are unconditionally and irrevocably guaranteed by each other Obligor pursuant to the Security Agreement. Each such guarantee constitutes a direct and unconditional obligation of such Obligor secured in the manner described in Condition 4.

**(d) Bond Policy issued by Financial Guarantor**

*This Condition 3(d) is applicable only in relation to Bonds which are specified as being Class A Wrapped Bonds or Class B Wrapped Bonds.*

Class A Wrapped Bonds and Class B Wrapped Bonds will each have the benefit of a Bond Policy issued by a Financial Guarantor specified in the applicable Final Terms, issued pursuant to an insurance and indemnity agreement between the Issuer, AWS and the relevant Financial Guarantor dated on or before the Issue Date (each an “**I&I Agreement**”) of such Bonds. Under the relevant Bond Policy, the relevant Financial Guarantor unconditionally and irrevocably agrees to pay to the Bond Trustee all sums due and repayable but unpaid by the Issuer in respect of scheduled interest and payment of principal (adjusted for indexation in accordance with these Terms and Conditions but excluding always the FG Excepted Amounts) on such Class A Wrapped Bonds or Class B Wrapped Bonds, all as more particularly described in the relevant Bond Policy. However, the Issuer is required to draw upon certain liquidity facilities available to it before the relevant Financial Guarantor is required to pay under the relevant Bond Policy.

The terms of the relevant Bond Policy provide that amounts of principal on any such Bonds which have become immediately due and payable (whether by virtue of acceleration, prepayment or otherwise) other than on a relevant Payment Day (as defined under such Bond Policy) will not be treated as Insured Amounts (as defined in such Bond Policy) which are Due for Payment (as defined in such Bond Policy) under such Bond Policy unless the relevant Financial Guarantor in its sole discretion elects to do so by notice in writing to the Bond Trustee. If no such election is made, the relevant Financial Guarantor will continue to be liable to make payments in respect of the Bonds pursuant to the relevant Bond Policy on the dates on which such payments would have been required to be made if such amounts had not become immediately due and repayable.

**To the extent that the Early Redemption Amount (as referred to in Condition 10(e)) or the Optional Redemption Amount (as referred to in Condition 10(d)), of any Bonds exceeds the aggregate of the outstanding nominal amount of and any accrued interest outstanding on any such Bonds to be redeemed, payment of such Early Redemption Amount or, as the case may be, such Optional Redemption Amount, will not be guaranteed by the relevant Financial Guarantor under the relevant Bond Policy.**

**(e) Status of Bond Policy**

*This Condition 3(e) is applicable only in relation to Bonds which are specified as being Class A Wrapped Bonds or Class B Wrapped Bonds.*

The relevant Bond Policy provided by the relevant Financial Guarantor in respect of the Bonds will constitute a direct and unconditional obligation of the relevant Financial Guarantor which will rank *pari passu* with all other unsecured obligations of such Financial Guarantor, save for such obligations as may be preferred by provisions of law that are both mandatory and of general application.

#### **4. SECURITY, PRIORITY AND RELATIONSHIP WITH SECURED CREDITORS**

##### **(a) Security**

Under the Security Agreement, each Obligor guarantees the obligations of each other Obligor under the Finance Documents to the Security Trustee for itself and on behalf of the Secured Creditors (including, without limitation, Bondholders) and secures such obligations upon the whole of its property, undertaking and assets, subject to certain specified exceptions and, in the case of AWS, to the terms of the Instrument of Appointment (as defined below) and any requirements thereunder or the Act (as defined below). There is no intention to create further security for the benefit of the holders of Bonds issued after the first Series. Each further Series of Bonds issued by the Issuer and any additional creditor of the Issuer acceding to the STID will share in the Security.

In these Conditions:

the “**Act**” means the United Kingdom Water Industry Act 1991 (as amended); and

“**Instrument of Appointment**” means the instrument of appointment dated 1989 under which the Secretary of State for the Environment appointed AWS as a water and sewerage undertaker under the Act for the areas described in the Instrument of Appointment, as modified or amended from time to time.

##### **(b) Relationship among Bondholders and with other Secured Creditors**

The Bond Trust Deed contains provisions detailing the Bond Trustee’s obligations to consider the interests of the Bondholders as regards all powers, trusts and authorities, duties and discretions of the Bond Trustee (except where expressly provided or otherwise referred to in Condition 20).

The STID provides that the Security Trustee (except in relation to its Reserved Matters and Entrenched Rights and subject to certain exceptions) will act on instructions of the Majority Creditors (as defined in the Master Definitions Agreement) (including the Bond Trustee as trustee for and representative of the holders of each Series of Wrapped Bonds (following the occurrence of an FG Event of Default in respect of the Financial Guarantor of those Wrapped Bonds which is continuing) and the Unwrapped Bondholders) (other than the USPP Bondholders) and, when so doing, the Security Trustee is not required to have regard to the interests of any Secured Creditor (including the Bond Trustee as trustee for and representative of the Bondholders or any individual Bondholder) in relation to the exercise of such rights and, consequently, has no liability to the Bondholders as a consequence of so acting.

##### **(c) Enforceable Security**

In the event of the Security becoming enforceable as provided in the STID, the Security Trustee shall, if instructed by the Majority Creditors, enforce its rights with respect to the Security, but without any liability as to the consequence of such action and without having regard to the effect thereof on, or being required to account for such action to, any particular Secured Creditor (including the Bond Trustee as trustee for the Bondholders or any individual Bondholder), provided that the Security Trustee shall not be obliged to take any action unless it is indemnified and/or secured to its satisfaction.

##### **(d) Application After Enforcement**

After enforcement of the Security, the Security Trustee shall (to the extent that such funds are available) use funds standing to the credit of the Accounts to make payments in accordance with the Payment Priorities (as set out in the Common Terms Agreement).

##### **(e) Bond Trustee and Security Trustee not liable for security**

The Bond Trustee and the Security Trustee will not be liable for any failure to make the usual investigations or any investigations which might be made by a security holder in relation to the property which is the subject of the Security, and shall not be bound to enquire into or be liable for any defect or failure in the right or title of the relevant Obligor to the Security, whether such defect or failure was known to the Bond Trustee or the Security Trustee or might have been discovered upon examination or enquiry or whether capable of remedy or not, nor will it have any liability for the enforceability of the Security created under the Security Documents whether as a result of any failure, omission or defect in registering or filing or otherwise protecting or perfecting such Security. The Bond Trustee and the Security Trustee have no responsibility for the value of any such Security.



## 5. ISSUER COVENANTS

So long as any of the Bonds remain outstanding, the Obligors have agreed to comply with the covenants as set out in Schedule 5 of the Common Terms Agreement.

The Bond Trustee is entitled to rely absolutely on a certificate of any two directors of the Issuer or any other Obligor in relation to any matter relating to the Covenants and to accept without liability any such certificate as sufficient evidence of the relevant fact or matter stated in such certificate.

The Covenants include, subject, in some cases, to certain materiality qualifications, exceptions and reservations as to matters of law, covenants as to how AWS will carry on its business, including restrictions upon each Obligor's ability to dispose of its assets, create security, grant guarantees, incur further financial indebtedness and amend any Material Agreement. *Details of the covenants to be given by the Obligors, and those to be given by AWS and the Issuer are summarised in Chapter 7, "Financing Structure – Common Terms Agreement, Information – Covenants, Covenants – General, Financial Covenants".*

The Common Terms Agreement also prescribes the manner in which AWS must manage its cash resources and the order in which it must pay its liabilities. See Chapter 7, "Financing Structure – Common Terms Agreement" and "Cash Management".

## 6. REDENOMINATION

### (a) Redenomination

Where redenomination is specified in the applicable Final Terms as being applicable, the Issuer may, without the consent of the Bondholders, the Receiptholders and the Couponholders, on giving prior notice to the Agent, Euroclear and Clearstream, Luxembourg and at least 30 days' prior notice to the Bondholders in accordance with Condition 18, elect that, with effect from the Redenomination Date specified in the notice, the Bonds shall be redenominated in euro.

The election will have effect as follows:

- (i) the Bonds and the Receipts shall be deemed to be redenominated in euro in the denomination of euro 0.01 with a nominal amount for each Bond and Receipt equal to the nominal amount of that Bond or Receipt in the Specified Currency, converted into euro at the Established Rate, provided that, if the Issuer determines, with the agreement of the Principal Paying Agent, that the then market practice in respect of the redenomination in euro of internationally offered securities is different from the provisions specified above, such provisions shall be deemed to be amended so as to comply with such market practice and the Issuer shall promptly notify the Bondholders, the stock exchange (if any) on which the Bonds may be listed and the Paying Agents of such deemed amendments;
- (ii) save to the extent that an Exchange Notice has been given in accordance with paragraph (iv) below, the amount of interest due in respect of the Bonds will be calculated by reference to the aggregate nominal amount of Bonds presented (or, as the case may be, in respect of which Coupons are presented) for payment by the relevant holder and the amount of such payment shall be rounded down to the nearest euro 0.01;
- (iii) if definitive Bonds are required to be issued after the Redenomination Date, they shall be issued at the expense of the Issuer in the denominations of euro 1,000, euro 10,000, euro 100,000 and (but only to the extent of any remaining amounts less than euro 1,000 or such smaller denominations as the Principal Paying Agent may approve) euro 0.01 and such other denominations as the Principal Paying Agent shall determine and notify to the Bondholders;
- (iv) if issued prior to the Redenomination Date, all unmatured Coupons denominated in the Specified Currency (whether or not attached to the Bonds) will become void with effect from the date on which the Issuer gives notice (the "Exchange Notice") that replacement euro-denominated Bonds, Receipts and Coupons are available for exchange (provided that such securities are so available) and no payments will be made in respect of them. The payment obligations contained in any Bonds and Receipts so issued will also become void on that date although those Bonds and Receipts will continue to constitute valid exchange obligations of the Issuer. New euro-denominated Bonds, Receipts and Coupons will be issued in exchange for Bonds, Receipts and

Coupons denominated in the Specified Currency in such manner as the Agent may specify and as shall be notified to the Bondholders in the Exchange Notice. No Exchange Notice may be given less than 15 days prior to any date for payment of principal or interest on the Bonds;

- (v) after the Redenomination Date, all payments in respect of the Bonds, the Receipts and the Coupons, other than payments of interest in respect of periods commencing before the Redenomination Date, will be made solely in euro as though references in the Bonds to the Specified Currency were to euro. Payments will be made in euro by credit or transfer to a euro account (or any other account to which euro may be credited or transferred) specified by the payee or, at the option of the payee, by a euro cheque;
- (vi) if the Bonds are Fixed Rate Bonds and interest for any period ending on or after the Redenomination Date is required to be calculated for a period ending other than on an Interest Payment Date, it will be calculated by applying the Rate of Interest to each Specified Denomination, multiplying such sum by the applicable Day Count Fraction, and rounding the resultant figure to the nearest sub-unit of the relevant Specified Currency, half of any such sub-unit being rounded upwards or otherwise in accordance with applicable market convention; and
- (vii) if the Bonds are Floating Rate Bonds or Index-Linked Bonds, the applicable Final Terms will specify any relevant changes to the provisions relating to interest.

**(b) Definitions**

In the Conditions, the following expressions have the following meanings:

“**Established Rate**” means the rate for the conversion of the Specified Currency (including compliance with rules relating to roundings in accordance with applicable European Community regulations) into euro established by the Council of the European Union pursuant to Article 123 of the Treaty;

“**euro**” means the currency introduced at the start of the third stage of European economic and monetary union pursuant to the Treaty;

“**Redenomination Date**” means (in the case of interest bearing Bonds) any date for payment of interest under the Bonds or (in the case of Zero Coupon Bonds) any date, in each case specified by the Issuer in the notice given to the Noteholders pursuant to paragraph (a) above and which falls on or after the date on which the country of the Specified Currency first participates in the third stage of European economic and monetary union; and

“**Treaty**” means the Treaty establishing the European Community, as amended.

**7. INTEREST**

**(a) Interest on Fixed Rate Bonds and Indexation Bonds**

Each Fixed Rate Bond and Indexation Bond bears interest on its outstanding nominal amount (or, if it is a Partly Paid Bond, the amount paid up) and, if it is an Indexation Bond, adjusted for indexation in accordance with Condition 9) from (and including) the Interest Commencement Date at the rate(s) per annum equal to the Rate(s) of Interest. Interest will be payable in arrear on the Interest Payment Date(s) in each year up to (and including) the Maturity Date.

Except as provided in the applicable Final Terms, the amount of interest payable on each Interest Payment Date in respect of the Fixed Interest Period ending on (but excluding) such date will amount to the Fixed Coupon Amount. Payments of interest on any Interest Payment Date will, if so specified in the applicable Final Terms, amount to the Broken Amount so specified.

As used in these Terms and Conditions, “**Fixed Interest Period**” means the period from (and including) an Interest Payment Date (or the Interest Commencement Date) to (but excluding) the next (or first) Interest Payment Date.

If interest is required to be calculated for a period other than a Fixed Interest Period, such interest shall be calculated (i) in the case of Bonds other than Indexation Bonds, by applying the Rate of Interest to each Specified Denomination, multiplying such sum by the applicable Day Count Fraction, and rounding the resultant figure to the nearest sub-unit of the relevant Specified Currency, half of any such sub-unit being rounded upwards or otherwise in accordance with applicable market convention and (ii) in the case of

Indexation Bonds, on an actual/actual basis in line with the method used by the Debt Management Office for the United Kingdom Index-Linked Gilt Edged Market.

“**Day Count Fraction**” means, in respect of the calculation of an amount of interest, in accordance with this Condition 7(a):

- (i) if “**Actual/Actual (ICMA)**” is specified in the applicable Final Terms:
  - (A) in the case of Bonds where the number of days in the relevant period from (and including) the most recent Interest Payment Date (or, if none, the Interest Commencement Date) to (but excluding) the relevant payment date (the “**Accrual Period**”) is equal to or shorter than the Determination Period during which the Accrual Period ends, the number of days in such Accrual Period divided by the product of (1) the number of days in such Determination Period and (2) the number of Determination Dates (as specified in the applicable Final Terms) that would occur in one calendar year; or
  - (B) in the case of Bonds where the Accrual Period is longer than the Determination Period, during which the Accrual Periods ends, the sum of:
    - (1) the number of days in such Accrual Period falling in the Determination Period in which the Accrual Period begins divided by the product of (x) the number of days in such Determination Period and (y) the number of Determination Dates (as specified in the applicable Final Terms) that would occur in one calendar year; and
    - (2) the number of days in such Accrual Period falling in the next Determination Period divided by the product of (x) the number of days in such Determination Period and (y) the number of Determination Dates that would occur in one calendar year; and
- (ii) if “**30/360**” is specified in the applicable Final Terms, the number of days in the period from (and including) the most recent Interest Payment Date (or, if none, the Interest Commencement Date) to (but excluding) the relevant payment date (such number of days being calculated on the basis of a year of 360 days with 12 30-day months) divided by 360.

In these Terms and Conditions:

“**Determination Period**” means each period from (and including) a Determination Date to (but excluding) the next Determination Date (including, where either the Interest Commencement Date or the final Interest Payment Date is not a Determination Date, the period commencing on the first Determination Date prior to, and ending on the first Determination Date falling after, such date); and

“**sub-unit**” means with respect to any currency other than euro, the lowest amount of such currency that is available as legal tender in the country of such currency and, with respect to euro, means one cent.

**(b) Interest on Floating Rate Bonds and Index Linked Interest Bonds**

(i) Interest Payment Dates

Each Floating Rate Bond and Index Linked Interest Bond bears interest on its outstanding nominal amount (or, if it is a Partly Paid Bond, the amount paid up) from (and including) the Interest Commencement Date and such interest will be payable in arrear on either:

- (A) the Specified Interest Payment Date(s) in each year specified in the applicable Final Terms; or
- (B) if not express Specified Interest Payment Date(s) is/are specified in the applicable Final Terms, each date (each such date, together with each Specified Interest Payment Date, an “**Interest Payment Date**”) which falls the number of months or other period specified as the Specified Period in the applicable Final Terms after the preceding Interest Payment Date or, in the case of the first Interest Payment Date, after the Interest Commencement Date.

Such interest will be payable in respect of each Interest Period (which expression shall, in these Conditions, mean the period from (and including) an Interest Payment Date (or the Interest Commencement Date) to (but excluding) the next (or first) Interest Payment Date).

If a Business Day Convention is specified in the applicable Final Terms and (x) if there is no numerically corresponding day on the calendar month in which an Interest Payment Date should occur or (y) if any Interest Payment Date would otherwise fall on a day which is not a Business Day, then, if the Business Day Convention specified is:

- (1) in any case where Specified Periods are specified in accordance with Condition 7(b)(i)(B) above, the Floating Rate Convention, such Interest Payment Date (i) in the case of (x) above, shall be the last day that is a Business Day in the relevant month and the provisions of (B) below shall apply, *mutatis mutandis*, or (ii) in the case of (y) above, shall be postponed to the next day which is a Business Day unless it would thereby fall into the next calendar month, in which event (A) such Interest Payment Date shall be brought forward to the immediately preceding Business Day and (B) each subsequent Interest Payment Date shall be the last Business Day in the month which falls in the Specified Period after the preceding applicable Interest Payment Date occurred; or
- (2) the Following Business Day Convention, such Interest Payment Date shall be postponed to the next day which is a Business Day; or
- (3) the Modified Following Business Day Convention, such Interest Payment Date shall be postponed to the next day which is a Business Day unless it would thereby fall into the next calendar month, in which event such Interest Payment Date shall be brought forward to the immediately preceding Business Day; or
- (4) the Preceding Business Day Convention, such Interest Payment Date shall be brought forward to the immediately preceding Business Day.

In these Conditions, “**Business Day**” means a day which is both:

- (A) a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in London and any Additional Business Centre specified in the applicable Final Terms; and
  - (B) either (1) in relation to any sum payable in a Specified Currency other than euro, a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in the principal financial centre of the country of the relevant Specified Currency (if other than London and any Additional Business Centre and which if the Specified Currency is Australian dollars or New Zealand dollars shall be Sydney and Auckland, respectively) or (2) in relation to any sum payable in euro, a day on which the Trans-European Automated Real-Time Gross Settlement Express Transfer (TARGET) System (the “**TARGET System**”) is open.
- (ii) Rate of Interest

The Rate of Interest payable from time to time in respect of Floating Rate Bonds and Index Linked Interest Bonds will be determined in the manner specified in the applicable Final Terms.

- (A) ISDA Determination for Floating Rate Bonds

Where ISDA Determination is specified in the applicable Final Terms as the manner in which the Rate of Interest is to be determined, the Rate of Interest for each Interest Period will be the relevant ISDA Rate plus or minus (as indicated in the applicable Final Terms) the Margin (if any). For the purposes of this sub-paragraph (A), “**ISDA Rate**” for an Interest Period means a rate equal to the Floating Rate that would be determined by the Principal Paying Agent under an interest rate swap transaction if the Principal Paying Agent were acting as Calculation Agent for that swap transaction under the terms of an agreement incorporating the 2000 ISDA Definitions, as published by the International

Swaps and Derivatives Associations, Inc. and as amended and updated as at the Issue Date of the first Tranche of the Bonds, published by the International Swaps and Derivatives Association, Inc. (the “**ISDA Definitions**”) and under which:

- (1) the Floating Rate Option is as specified in the applicable Final Terms;
- (2) the Designated Maturity is a period specified in the applicable Final Terms; and
- (3) the relevant Reset Date is either (i) if the applicable Floating Rate Option is based on the London inter-bank offered rate (“LIBOR”) or on the Euro-zone inter-bank offered rate (“EURIBOR”), the first day of that Interest Period or (ii) in any other case, as specified in the applicable Final Terms.

For the purposes of this sub-paragraph (A), “**Floating Rate**”, “**Calculation Agent**”, “**Floating Rate Option**”, “**Designated Maturity**” and “**Reset Date**” have the meanings given to those terms in the ISDA Definitions.

(B) Screen Rate Determination for Floating Rate Bonds

Where Screen Rate Determination is specified in the applicable Final Terms as the manner in which the Rate of Interest is to be determined, the Rate of Interest for each Interest Period will, subject as provided below, be either:

- (1) the offered quotation; or
- (2) the arithmetic mean (rounded if necessary to the fifth decimal place, with 0.000005 being rounded upwards) of the offered quotations,

(expressed as a percentage rate per annum) for the Reference Rate which appears or appear, as the case may be, on the Relevant Screen Page as at 11.00 a.m. (London time, in the case of LIBOR, or Brussels time, in the case of EURIBOR) (the “**Specified Time**”) on the Interest Determination Date in question plus or minus (as indicated in the applicable Final Terms) the Margin (if any), all as determined by the Principal Paying Agent. If five or more of such offered quotations are available on the Relevant Screen Page, the highest (or, if there is more than one such highest quotation, one only of such quotations) and the lowest (or, if there is more than one such lowest quotation, one only of such quotations) shall be disregarded by the Principal Paying Agent for the purpose of determining the arithmetic mean (rounded as provided above) of such offered quotations.

If the Relevant Screen Page is not available or if, in the case of (1) above, no offered quotation appears or, in the case of (2) above, fewer than three offered quotations appear, in each case as at the Specified Time on the Interest Determination Date in question, the Principal Paying Agent shall request each of the Reference Banks to provide the Principal Paying Agent with its offered quotation (expressed as a percentage rate per annum) for the Reference Rate at approximately the Specified Time on the Interest Determination Date in question. If two or more of the Reference Banks provide the Principal Paying Agent with offered quotations, the Rate of Interest for the Interest Period shall be the arithmetic mean (rounded if necessary to the fifth decimal place, with 0.000005 being rounded upwards) of the offered quotations plus or minus (as appropriate) the Margin (if any), all as determined by the Principal Paying Agent.

If on any Interest Determination Date one only or none of the Reference Banks provides the Principal Paying Agent with an offered quotation as provided in the preceding paragraph, the Rate of Interest for the relevant Interest Period shall be the rate per annum which the Principal Paying Agent determines as being the arithmetic mean (rounded if necessary to the fifth decimal place, with 0.000005 being rounded upwards) of the rates, as communicated to (and at the request of) the Principal Paying Agent by the Reference Banks or any two or more of them, at which such banks were offered, at approximately the Specified Time on the relevant Interest Determination Date, deposits in the Specified Currency for a period equal to that which would have been used for the Reference Rate by leading banks in the London inter-bank market (if the Reference Rate is LIBOR) or the Euro-zone inter-bank market (if the Reference Rate is EURIBOR) plus or minus (as

appropriate) the Margin (if any) or, if fewer than two of the Reference Banks provide the Principal Paying Agent with offered rates, the offered rate for deposits in the Specified Currency for a period equal to that which would have been used for the Reference Rate, or the arithmetic mean (rounded as provided above) of the offered rates for deposits in the Specified Currency for a period equal to that which would have been used for the Reference Rate, at which, at approximately the Specified Time on the relevant Interest Determination Date, any one or more banks (which bank or banks is or are in the opinion of the Issuer suitable for the purpose) informs the Principal Paying Agent it is quoting to leading banks in the London inter-bank market (if the Reference Rate is LIBOR) or the Euro-zone inter-bank market (if the Reference Rate is EURIBOR) plus or minus (as appropriate) the Margin (if any), provided that, if the Rate of Interest cannot be determined in accordance with the foregoing provisions of this paragraph, the Rate of Interest shall be determined as at the last preceding Interest Determination Date (though substituting, where a different Margin is to be applied to the relevant Interest Period from that which applied to the last preceding Interest Period, the Margin relating to the relevant Interest Period in place of the Margin relating to that last preceding Interest Period).

If the Reference Rate from time to time in respect of Floating Rate Bonds is specified in the applicable Final Terms as being other than LIBOR or EURIBOR, the Rate of Interest in respect of such Bonds will be determined as provided in the applicable Final Terms.

(i) Minimum Rate of Interest and/or Maximum Rate of Interest

If the applicable Final Terms specify a Minimum Rate of Interest for any Interest Period, then, in the event that the Rate of Interest in respect of such Interest Period determined in accordance with the provisions of paragraph (ii) above is less than such Minimum Rate of Interest, the Rate of Interest for such Interest Period shall be such Minimum Rate of Interest.

If the applicable Final Terms specify a Maximum Rate of Interest for any Interest Period, then, in the event that the Rate of Interest in respect of such Interest Period determined in accordance with the provisions of paragraph (ii) above is greater than such Maximum Rate of Interest, the Rate of Interest for such Interest Period shall be such Maximum Rate of Interest.

(ii) Determination of Rate of Interest and calculation of Interest Amounts

The Principal Paying Agent, in the case of Floating Rate Bonds, and the Calculation Agent, in the case of Index Linked Interest Bonds, will at or as soon as practicable after each time at which the Rate of Interest is to be determined, determine the Rate of Interest for the relevant Interest Period. In the case of Index Linked Interest Bonds, the Calculation Agent will notify the Principal Paying Agent of the Rate of Interest for the relevant Interest Period as soon as practicable after calculating the same.

The Principal Paying Agent will calculate the amount of interest (the “**Interest Amount**”) payable on the Floating Rate Bonds or Index Linked Interest Bonds in respect of each Specified Denomination for the relevant Interest Period. Each Interest Amount shall be calculated by applying the Rate of Interest to each Specified Denomination, multiplying such sum by the applicable Day Count Fraction, and rounding the resultant figure to the nearest sub-unit of the relevant Specified Currency, half of any such sub-unit being rounded upwards or otherwise in accordance with applicable market convention.

“**Day Count Fraction**” means, in respect of the calculation of an amount of interest in accordance with this Condition 7(b):

- (A) if “Actual/365” or “Actual/Actual-ISDA” is specified in the applicable Final Terms, the actual number of days in the Interest Period divided by 365 (or, if any portion of that Interest Period falls in a leap year, the sum of (A) the actual number of days in that portion of the Interest Period falling in a leap year divided by 366 and (B) the actual number of days in that portion of the Interest Period falling in a non-leap year divided by 365);
- (B) if “Actual/365 (Fixed)” is specified in the applicable Final Terms, the actual number of days in the Interest Period divided by 365;

- (C) if “Actual/365 (Sterling)” is specified in the applicable Final Terms, the actual number of days in the Interest Period divided by 365 or, in the case of an Interest Payment Date falling in a leap year, 366;
- (D) if “Actual/360” is specified in the applicable Final Terms, the actual number of days in the Interest Period divided by 360;
- (E) if “30/360”, “360/360” or “Bond Basis” is specified in the applicable Final Terms, the number of days in the Interest Period divided by 360 (the number of days to be calculated on the basis of a year of 360 days with 12 30-day months (unless (x) the last day of the Interest Period is the 31st day of a month but the first day of the Interest Period is a day other than the 30th or 31st day of a month, in which case the month that includes that last day shall not be considered to be shortened to a 30-day month, or (y) the last day of the Interest Period is the last day of the month of February in which case the month of February shall not be considered to be lengthened to a 30-day month)); and
- (F) if “30E/360” or “Eurobond Basis” is specified in the applicable Final Terms, the number of days in the Interest Period divided by 360 (the number of days to be calculated on the basis of a year of 360 days with 12 30-day months, without regard to the date of the first day or last day of the Interest Period unless, in the case of the final Interest Period, the Maturity Date is the last day of the month of February, in which case the month of February shall not be considered to be lengthened to a 30-day month).

(iii) Notification of Rate of Interest and Interest Amounts

The Principal Paying Agent will cause the Rate of Interest and each Interest Amount for each Interest Period and the relevant Interest Payment Date to be notified to the Issuer and the other Obligors, the Bond Trustee and any stock exchange or other relevant authority on which the relevant Floating Rate Bonds or Index Linked Interest Bonds are for the time being listed or by which they have been admitted to listing and notice thereof to be published in accordance with Condition 18 as soon as possible after their determination but in no event later than the fourth London Business Day thereafter. Each Interest Amount and Interest Payment Date so notified may subsequently be amended (or appropriate alternative arrangements made by way of adjustment) without prior notice in the event of an extension or shortening of the Interest Period. Any such amendment will be promptly notified to each stock exchange or other relevant authority on which the relevant Floating Rate Bonds or Index Linked Interest Bonds are for the time being listed or by which they have been admitted to listing and to the Bondholders in accordance with Condition 18. For the purposes of this paragraph, the expression “**London Business Day**” means a day (other than a Saturday or a Sunday) on which banks and foreign exchange markets are open for general business in London.

(iv) Determination or calculation by the Bond Trustee

If for any reason at any time the Principal Paying Agent or, as the case may be, the Calculation Agent defaults in its obligations to determine the Rate of Interest or the Principal Paying Agent defaults in its obligation to calculate any Interest Amount in accordance with sub-paragraph (ii) (A) or (B) above, as the case may be, and in each case, (iv) above, the Bond Trustee shall determine the Rate of Interest at such rate as, in its absolute discretion (having regard as it shall think fit to the foregoing provisions of this Condition, but subject always to any Minimum or Maximum Rate of Interest specified in the applicable Final Terms), it shall deem fair and reasonable in all the circumstances or, as the case may be, the Bond Trustee shall calculate the Interest Amount(s) in such manner as it shall deem fair and reasonable in all the circumstances and each such determination or calculation shall be deemed to have been made by the Principal Paying Agent or the Calculation Agent, as applicable.

(v) Certificates to be final

All certificates, communications, opinions, determinations, calculations, quotations and decisions given, expressed, made or obtained for the purposes of the provisions of this Condition 7(b), whether by the Principal Paying Agent or, if applicable, the Calculation Agent or the Bond Trustee, shall (in the absence of wilful default, bad faith or manifest error) be binding on the Issuer, the Obligors, the Bond Trustee, the Principal Paying Agent, the Calculation Agent (if

applicable), the other Agents and all Bondholders, Receiptholders and Couponholders and (in the absence as aforesaid) no liability to the Issuer, the Obligors, the Bond Trustee, the Bondholders, the Receiptholders or the Couponholders shall attach to the Principal Paying Agent or, if applicable, the Calculation Agent or the Bond Trustee in connection with the exercise or non-exercise by it of its powers, duties and discretions pursuant to such provisions.

**(c) Interest on Dual Currency Interest Bonds**

The rate or amount of interest payable in respect of Dual Currency Interest Bonds shall be determined in the manner specified in the applicable Final Terms.

**(d) Interest on Partly Paid Bonds**

In the case of Partly Paid Bonds (other than Partly Paid Bonds which are Zero Coupon Bonds), interest will accrue as aforesaid on the paid-up nominal amount of such Bonds and otherwise as specified in the applicable Final Terms.

**(e) Accrual of interest**

Each Bond (or in the case of the redemption of part only of a Bond, that part only of such Bond) will cease to bear interest (if any) from the date for its redemption unless, upon due presentation thereof, payment of principal is improperly withheld or refused. In such event, interest will continue to accrue as provided in the Bond Trust Deed.

**(f) Deferral of interest on Class B Bonds**

*This Condition 7(f) is applicable only in relation to Bonds which are specified as being Class B Bonds.*

In the case of Class B Bonds only, if, on any Interest Payment Date, prior to delivery of an enforcement notice under Condition 13, there are insufficient funds available to pay any accrued interest on such Class B Bonds, such accrued interest will be treated as not having fallen due and will be deferred in accordance with the cash management provisions contained in Schedule 12 of the Common Terms Agreement (“**Deferred Interest**”) until the earlier of (i) the next succeeding Interest Payment Date for those Class B Bonds on which the Issuer has, in accordance with the cash management provisions contained in Schedule 12 of the Common Terms Agreement, sufficient funds available to pay such Deferred Interest (including any interest accrued thereon); and (ii) the date on which all the Class A Debt (as defined in the Master Definitions Agreement) is repaid in full. Interest will continue to accrue on such Deferred Interest at the Rate of Interest otherwise payable on unpaid principal of such Class B Bonds.

**8. PAYMENTS**

**(a) Method of payment**

Subject as provided below:

- (i) payments in a Specified Currency other than euro will be made by credit or transfer to an account in the relevant Specified Currency (which, in the case of a payment in Japanese yen to a non-resident of Japan, shall be a non-resident account) maintained by the payee with, or, at the option of the payee, by a cheque in such Specified Currency drawn on, a bank in the principal financial centre of the country of such Specified Currency (which, if the Specified Currency is Australian dollars or New Zealand dollars, shall be Sydney and Auckland, respectively); and
- (ii) payments in euro will be made by credit or transfer to a euro account (or any other account to which euro may be credited or transferred) specified by the payee or, at the option of the payee, by a euro cheque.
- (iii) Payments will be subject in all cases to any fiscal or other laws and regulations applicable thereto in the place of payment, but without prejudice to the provisions of Condition 11.

**(b) Presentation of definitive Bearer Bonds, Receipts and Coupons**

Payments of principal in respect of definitive Bearer Bonds will (subject as provided below) be made in the manner provided in paragraph (a) above only against presentation and surrender (or, in the case of part payment of any sum due, endorsement) of definitive Bearer Bonds, and payments of interest in respect of definitive Bearer Bonds will (subject as provided below) be made as aforesaid only against presentation



and surrender (or, in the case of part payment of any sum due, endorsement) of Coupons, in each case at the specified office of any Paying Agent outside the United States (which expression, as used herein, means the United States of America (including the States and the District of Columbia, its territories, its possessions and other areas subject to its jurisdiction)).

Payments of instalments of principal (if any) in respect of definitive Bearer Bonds, other than the final instalment, will (subject as provided below) be made in the manner provided in paragraph (a) above against presentation and surrender (or, in the case of part payment of any sum due, endorsement) of the relevant Receipt in accordance with the preceding paragraph. Payment of the final instalment will be made in the manner provided in paragraph (a) above only against presentation and surrender (or, in the case of part payment of any sum due, endorsement) of the relevant Bearer Bond in accordance with the preceding paragraph. Each Receipt must be presented for payment of the relevant instalment together with the definitive Bearer Bond to which it appertains. Receipts presented without the definitive Bearer Bond to which they appertain do not constitute valid obligations of the Issuer. Upon the date on which any definitive Bearer Bond becomes due and repayable, unmatured Receipts (if any) relating thereto (whether or not attached) shall become void and no payment shall be made in respect thereof.

Fixed Rate Bonds in definitive bearer form (other than Dual Currency Bonds, Index Linked Interest Bonds, Indexation Bonds or Long Maturity Bonds (as defined below)) should be presented for payment together with all unmatured Coupons appertaining thereto (which expression shall for this purpose include Coupons falling to be issued on exchange of matured Talons), failing which the amount of any missing unmatured Coupon (or, in the case of payment not being made in full, the same proportion of the amount of such missing unmatured Coupon as the sum so paid bears to the sum due) will be deducted from the sum due for payment. Each amount of principal so deducted will be paid in the manner mentioned above against surrender of the relative missing Coupon at any time before the expiry of 10 years after the Relevant Date (as defined in Condition 12) in respect of such principal (whether or not such Coupon would otherwise have become void under Condition 12) or, if later, five years from the date on which such Coupon would otherwise have become due, but in no event thereafter.

Upon any Fixed Rate Bond in definitive bearer form becoming due and repayable prior to its Maturity Date, all unmatured Talons (if any) appertaining thereto will become void and no further Coupons will be issued in respect thereof.

Upon the date on which any Floating Rate Bond, Dual Currency Bond, Index Linked Interest Bond, Indexation Bond or Long Maturity Bond in definitive bearer form becomes due and repayable, unmatured Coupons and Talons (if any) relating thereto (whether or not attached) shall become void and no payment or, as the case may be, exchange for further Coupons shall be made in respect thereof. A "Long Maturity Bond" is a Fixed Rate Bond (other than a Fixed Rate Bond which on issue had a Talon attached) whose nominal amount on issue is less than the aggregate interest payable thereon provided that such Bond shall cease to be a Long Maturity Bond on the Interest Payment Date on which the aggregate amount of interest remaining to be paid after that date is less than the nominal amount of such Bond.

If the due date for redemption of any definitive Bearer Bond is not an Interest Payment Date, interest (if any) accrued in respect of such Bond from (and including) the preceding Interest Payment Date or, as the case may be, the Interest Commencement Date shall be payable only against surrender of the relevant definitive Bearer Bond.

**(c) Payments in respect of Bearer Global Bonds**

Payments of principal and interest (if any) in respect of Bonds represented by any Global Bond in bearer form will (subject as provided below) be made in the manner specified above in relation to definitive Bearer Bonds and otherwise in the manner specified in the relevant Global Bond against presentation or surrender, as the case may be, of such Global Bond at the specified office of any Paying Agent outside the United States. A record of each payment made against presentation or surrender of any Global Bond in bearer form, distinguishing between any payment of principal and any payment of interest, will be made on such Global Bond by the Paying Agent to which it was presented and such record shall be *prima facie* evidence that the payment in question has been made.

**(d) Payments in respect of Registered Bonds**

Payments of principal (other than instalments of principal prior to the final instalment) in respect of each Registered Bond (whether or not in global form) will be made against presentation and surrender (or, in

the case of part payment of any sum due, endorsement) of the Registered Bond at the specified office of the Registrar or any of the Paying Agents. Such payments will be made by transfer to the Designated Account (as defined below) of the holder (or the first named of joint holders) of the Registered Bond appearing in the register of holders of the Registered Bonds maintained by the Registrar (the “**Register**”) at the close of business on the third business day (being for this purpose a day on which banks are open for business in the city where the specified office of the Registrar is located) before the relevant due date. Notwithstanding the previous sentence, if (i) a holder does not have a Designated Account or (ii) the principal amount of the Bonds held by a holder is less than U.S.\$250,000 (or its approximate equivalent in any other Specified Currency), payment will instead be made by a cheque in the Specified Currency drawn on a Designated Bank (as defined below). For these purposes, “**Designated Account**” means the account (which, in the case of a payment in Japanese yen to a non-resident of Japan, shall be a non-resident account) maintained by a holder with a Designated Bank and identified as such in the Register and “**Designated Bank**” means (in the case of payment in a Specified Currency other than euro) a bank in the principal financial centre of the country of such Specified Currency (which, if the Specified Currency is Australian dollars or New Zealand dollars, shall be Sydney and Auckland, respectively) and (in the case of a payment in euro) any bank which processes payments in euro.

Payments of interest and payments of instalments of principal (other than the final instalment) in respect of each Registered Bond (whether or not in global form) will be made by a cheque in the Specified Currency drawn on a Designated Bank and mailed by uninsured mail on the business day in the city where the specified office of the Registrar is located immediately preceding the relevant due date to the holder (or the first named of joint holders) of the Registered Bond appearing in the Register at the close of business on the fifteenth day (whether or not such fifteenth day is a business day) before the relevant due date (the “**Record Date**”) at his address shown in the Register on the Record Date and at his risk. Upon application of the holder to the specified office of the Registrar not less than three business days in the city where the specified office of the Registrar is located before the due date for any payment of interest in respect of a Registered Bond, the payment may be made by transfer on the due date in the manner provided in the preceding paragraph. Any such application for transfer shall be deemed to relate to all future payments of interest (other than interest due on redemption) and instalments of principal (other than the final instalment) in respect of the Registered Bonds which become payable to the holder who has made the initial application until such time as the Registrar is notified in writing to the contrary by such holder. Payment of the interest due in respect of each Registered Bond on redemption and the final instalment of principal will be made in the same manner as payment of the principal amount of such Registered Bond.

Holders of Registered Bonds will not be entitled to any interest or other payment for any delay in receiving any amount due in respect of any Registered Bond as a result of a cheque posted in accordance with this Condition arriving after the due date for payment or being lost in the post. No commissions or expenses shall be charged to such holders by the Registrar in respect of any payments of principal or interest in respect of the Registered Bonds.

All amounts payable to DTC or its nominee as registered holder of a Registered Global Bond in registered form in respect of Bonds denominated in a Specified Currency other than U.S. dollars shall be paid by transfer by the Registrar to an account in the relevant Specified Currency of the Exchange Agent on behalf of DTC or its nominee for conversion into and payment in U.S. dollars in accordance with the provisions of the Agency Agreement.

None of the Issuer or the other Obligors, the Bond Trustee or the Agents will have any responsibility or liability for any aspect of the records relating to, or payments made on account of, beneficial ownership interests in the Registered Global Bonds or for maintaining, supervising or reviewing any records relating to such beneficial ownership interests.

**(e) General provisions applicable to payments**

The holder of a Global Bond shall be the only person entitled to receive payments in respect of Bonds represented by such Global Bond and the Issuer will be discharged by payment to, or to the order of, the holder of such Global Bond in respect of each amount so paid. Each of the persons shown in the records of Euroclear, Clearstream, Luxembourg or DTC as the beneficial holder of a particular nominal amount of Bonds represented by such Global Bond must look solely to Euroclear, Clearstream, Luxembourg or DTC, as the case may be, for his share of each payment so made by the Issuer to, or to the order of, the holder of such Global Bond.

Notwithstanding the foregoing provisions of this Condition, if any amount of principal and/or interest in respect of Bearer Bonds is payable in U.S. dollars, such U.S. dollar payments of principal and/or interest in respect of such Bond will be made at the specified office of a Paying Agent in New York City if:

- (i) the Issuer has appointed Paying Agents with specified offices outside the United States with the reasonable expectation that such Paying Agents would be able to make payment in U.S. dollars in the manner provided above when due;
- (ii) payment of the full amount of such principal and interest at all such specified offices outside the United States is illegal or effectively precluded by exchange controls or other similar restrictions on the full payment or receipt of principal and interest in U.S. dollars; and
- (iii) such payment is then permitted under United States law without involving, in the opinion of the Issuer, adverse tax consequences to the Issuer.

**(f) Payment Day**

If the date for payment of any amount in respect of any Bond, Receipt or Coupon is not a Payment Day, the holder thereof shall not be entitled to payment until the next following Payment Day and shall not be entitled to further interest or other payment in respect of such delay. For these purposes, “**Payment Day**” means any day which (subject to Condition 12) is:

- (i) either (A) in relation to any sum payable in a Specified Currency other than euro, a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in the principal financial centre of the country of the relevant Specified Currency (if other than the place of presentation, London and any Additional Financial Centre and which, if the Specified Currency is Australian dollars or New Zealand dollars, shall be Sydney and Auckland, respectively) or (B) in relation to any sum payable in euro, a day on which the TARGET System is open; and
- (ii) in the case of any payment in respect of a Registered Global Bond denominated in a Specified Currency other than U.S. dollars and registered in the name of DTC or its nominee and in respect of which an accountholder of DTC (with an interest in such Registered Global Bond) has elected to receive any part of such payment in U.S. dollars, a day on which commercial banks are not authorised or required by law or regulation to be closed in New York City.

**(g) Interpretation of principal and interest**

Any reference in these Conditions to principal in respect of the Bonds shall be deemed to include, as applicable:

- (i) any additional amounts which may be payable with respect to principal under Condition 11 or under any undertaking or covenant given in addition thereto or in substitution therefor pursuant to the Bond Trust Deed or the applicable Final Terms;
- (ii) the Final Redemption Amount of the Bonds;
- (iii) the Early Redemption Amount of the Bonds;
- (iv) the Optional Redemption Amount(s) (if any) of the Bonds;
- (v) in relation to Bonds redeemable in instalments, the Instalment Amounts;
- (vi) in relation to Zero Coupon Bonds, the Amortised Face Amount (as defined in Condition 10(e)); and
- (vii) any premium and any other amounts (other than interest) which may be payable by the Issuer under or in respect of the Bonds.

Any reference in these Conditions to interest in respect of the Bonds shall be deemed to include, as applicable, any additional amounts which may be payable with respect to interest under Condition 11 or under any undertaking or covenant given in addition thereto or in substitution therefor pursuant to the Bond Trust Deed or the applicable Final Terms.

## 9. INDEXATION

*The provisions of this Condition 9 apply only to Indexation Bonds.*

### (a) Definitions

In these Terms and Conditions:

“**Base Index Figure**” means, subject as provided in paragraph (c) below, the base index figure as specified in the applicable Final Terms;

“**Index**” or “**Index Figure**” means, subject as provided in paragraph (c) below, RPI (for all items) published by the Office for National Statistics (January 1987 = 100) or any comparable index which may replace such index for the purpose of calculating the amount payable on repayment of the Reference Gilt. Any reference to the Index Figure applicable to a particular month shall, subject as provided in paragraph (c) below, be construed as a reference to the Index Figure published in the seventh month prior to that particular month and relating to the month before that of publication;

“**Index Ratio**” applicable to any month means the Index Figure applicable to such month divided by the Base Index Figure; and

“**Reference Gilt**” means the reference gilt specified in the applicable Final Terms.

### (b) Application of the Index Ratio

Each payment of interest and principal in respect of the Bonds shall be the amount provided in or determined in accordance with these Conditions, multiplied by the Index Ratio applicable to the month in which such payment falls to be made and rounded to four decimal places (0.00005 being rounded upwards).

### (c) Changes in circumstances affecting the Index

(i) If at any time and from time to time the Index shall be changed by the substitution of a new base therefor, then with effect from, and including, the calendar month in which such substitution takes effect:

(A) the definition of “**Index**” and “**Index Figure**” shall be deemed to refer to the new date or month in substitution for January 1987 (or, as the case may be, such other date or month as may have been substituted therefor under this sub-paragraph (i)); and

(B) the new Base Index Figure shall be the product of the then existing Base Index Figure and the Index Figure immediately following such substitution, divided by the Index Figure immediately prior to such substitution.

(ii) If the Index Figure normally published in the seventh month, and relating to the eighth month (the “relevant month”), before the month in which a payment is due to be made is not published on or before the fourteenth Business Day before the date (the “date for payment”) on which such payment is due otherwise than because the Index has ceased to be published, the Index Figure applicable to the month in which the date for payment falls shall be:

(A) such substitute index figure (if any) as the Bond Trustee shall agree to have been published by the Bank of England for the purposes of indexation of payments on the Reference Gilt or, failing such publication, on any one or more issues of index-linked Treasury stock selected by the Bond Trustee on the advice of a gilt-edged market maker or other adviser selected by it in its sole discretion having consulted with the Issuer (but without responsibility or liability to the Issuer) (the “**Indexation Adviser**”); or

(B) if no such determination is made by the Indexation Adviser within seven days, the Index Figure last published (or, if later, the substitute index figure last determined pursuant to sub-paragraph (A) above before the date for payment).

Where the provisions of sub-paragraph (ii) above apply, the determination of the Indexation Adviser as to the Index Figure applicable to the month in which the date for payment falls shall be conclusive and binding. If, an Index Figure having been applied pursuant to sub-paragraph (B)

above, the Index Figure relating to the relevant month is subsequently published while a Bond is still outstanding, then:

- (x) in relation to a payment of principal or interest in respect of such Bond other than upon redemption in full of such Bond, the principal or interest (as the case may be) next payable after the date of such subsequent publication shall be increased or reduced by an amount equal to (respectively) the shortfall or excess of the amount of the relevant payment made on the basis of the Index Figure applicable by virtue of sub-paragraph (B) above either below or above the amount of the relevant payment that would have been due if the Index Figure subsequently published had been published on or before the fourteenth Business Day before the date for payment;
  - (y) in relation to a payment of principal or interest upon redemption in full of a Bond, no subsequent adjustment to amounts paid will be made.
- (iii) (A) If:
- (x) the Bond Trustee has been notified by the Principal Paying Agent that the Index has ceased to be published; or
  - (y) any change is made to the coverage or the basic calculation of the Index which constitutes a fundamental change which would, in the opinion of the Bond Trustee, acting solely on the advice of the Indexation Adviser, be materially prejudicial to the interests of the Bondholders,

the Bond Trustee will give written notice of such occurrence to the Issuer, and the Issuer and the Bond Trustee together shall seek to agree for the purpose of the Bonds one or more adjustments to the Index or a substitute index (with or without adjustments) with the intention that the same should leave the Issuer and the Bondholders in no better and no worse position than they would have been had the Index not ceased to be published or the relevant fundamental change not been made.

- (B) If the Issuer and the Bond Trustee fail to reach such agreement within 20 Business Days following the giving of such notice by the Bond Trustee, a bank or other person in London shall be appointed by the Issuer and the Bond Trustee, or, failing agreement on such appointment within 20 Business Days following the expiry of the 20 day period referred to above, by the Bond Trustee (in each case, such bank or other person so appointed being referred to as the “**Expert**”), to determine for the purpose of the Bonds one or more adjustments to the Index or a substitute index (with or without adjustments) with the intention that the same should leave the Issuer and the Bondholders in no better and no worse position than they would have been had the Index not ceased to be published or the relevant fundamental change not been made. Any Expert so appointed shall act as an expert and not as an arbitrator and all fees, costs and expenses of the Expert, the Issuer and the Bond Trustee in connection with such appointment shall be borne by the Issuer.
- (C) The Index shall be adjusted or replaced by a substitute index as agreed by the Issuer and the Bond Trustee or as determined by the Expert pursuant to the foregoing paragraphs, as the case may be, and references in these Conditions to the Index and to any Index Figure shall be deemed amended in such manner as the Bond Trustee may determine, and notify to the Issuer, as appropriate to give effect to such adjustment or replacement. Such amendments shall be effective from the date of such notification and binding upon the Issuer and the other Obligors, the Bond Trustee, the Financial Guarantors, the other Secured Creditors and the Bondholders and the Issuer shall give notice to the Bondholders in accordance with Condition 18 of such amendments as promptly as practicable following such notification.

## **10. REDEMPTION AND PURCHASE**

### **(a) Redemption at maturity**

Unless previously redeemed or purchased and cancelled as specified below, each Bond (including each Index Linked Redemption Bond and Dual Currency Redemption Bond) will be redeemed by the Issuer at its Final Redemption Amount (subject, in the case of Indexation Bonds, to adjustments for indexation in

accordance with Condition 9) specified in, or determined in the manner specified in, the applicable Final Terms in the relevant Specified Currency on the Maturity Date.

**(b) Early Redemption for Index Reasons**

If, in the case of Indexation Bonds, either:

- (i) the Index Figure fails to be determined for three consecutive months other than on the basis provided in Condition 9(c)(ii) and the Bond Trustee has been notified by the Principal Paying Agent that publication of the Index has ceased; or
- (ii) notice is published by Her Majesty's Treasury or on its behalf following a change in relation to the Index, offering a right of redemption to holders of the Reference Gilt,

and (in either case) no amendment or substitution of the Index shall have been advised by the Indexation Adviser to the Issuer, the Issuer may, on any Interest Payment Date upon which such circumstances are continuing, having given not more than 60 nor less than 30 days' notice to the Bond Trustee, the Security Trustee, the Majority Creditors and the holders of Indexation Bonds in accordance with Condition 18 (which notice shall be irrevocable) redeem all, but not some only, of the Indexation Bonds at their Early Redemption Amount, together with interest accrued up to and including the date of redemption.

**(c) Redemption for tax reasons**

In addition, if the Issuer satisfies the Bond Trustee that the Issuer would, on the next Interest Payment Date, become obliged to deduct or withhold from any payment of interest or principal in respect of the Bonds (other than in respect of default interest), any amount for or on account of any present or future taxes, duties, assessments or governmental charges of whatever nature imposed, levied, collected, withheld or assessed by the United Kingdom or any political subdivision thereof, or any other authority thereof or any change in the application or official interpretation of such laws or regulations, then the Issuer may in order to avoid the relevant deduction or withholding, use its reasonable endeavours to arrange substitution of a company incorporated in another jurisdiction approved by the Bond Trustee as principal debtor under the Bonds and as lender or creditor under the Intercompany Loan Arrangements upon satisfying the conditions for substitution of the Issuer as set out in the STID (and referred to in Condition 19). If the Issuer is unable to arrange a substitution as described above and, as a result, the relevant deduction or withholding is continuing then the Issuer may, except as otherwise provided in the applicable Final Terms, upon giving not more than 60 nor less than 30 days' notice to the Bond Trustee, the Security Trustee, the Majority Creditors and the Bondholders by the publication of a notice of redemption, in accordance with Condition 18, redeem all (but not some only) of the Bonds on any Interest Payment Date at their Early Redemption Amount plus accrued but unpaid interest thereon.

Prior to the publication of any notice of redemption pursuant to this Condition, the Issuer shall deliver to the Bond Trustee a certificate signed by two Directors of the Issuer stating that the Issuer is entitled to effect such redemption and setting forth a statement of facts showing that the conditions precedent to the right of the Issuer so to redeem have occurred. The Bond Trustee shall be entitled to accept such certificate as sufficient evidence of the satisfaction of such conditions precedent in which event they shall be conclusive and binding on the Bondholders, the Receiptholders and the Couponholders.

Bonds redeemed pursuant to this Condition 10(c) will be redeemed at their Early Redemption Amount referred to in paragraph (e) below together (if appropriate) with interest accrued to (but excluding) the date of redemption (adjusted, in the case of Indexation Bonds, for indexation in accordance with Condition 9 (the Index Ratio for this purpose being that applicable pursuant to Condition 9(c)(ii)(B) up to and including the date of redemption)).

**(d) Redemption at the option of the Issuer (Issuer Call)**

If Issuer Call is specified in the applicable Final Terms, the Issuer may, having given:

- (i) not less than 15 nor more than 30 days' notice to the Bondholders in accordance with Condition 18; and
- (ii) not less than 15 days before the giving of the notice referred to in (i), notice to the Principal Paying Agent and the Bond Trustee and, in the case of a redemption of Registered Bonds, the Registrar,

(which notices shall be irrevocable and shall specify the date fixed for redemption and, in the case of the USPP Bonds (as defined in Condition 10(k) below), such notice shall be accompanied by a certificate of a Director of the Issuer as to the estimated Make-Whole Amount due in connection with such redemption (calculated as if the date of such notice were the date of redemption) together with details of such computation), redeem all or some only of the Bonds then outstanding on any Optional Redemption Date and at the Optional Redemption Amount(s) specified in, or determined in the manner specified in, the applicable Final Terms together, if appropriate, with interest accrued to (but excluding) the relevant Optional Redemption Date. Any such redemption must be of a nominal amount not less than the Minimum Redemption Amount and not more than the Maximum Redemption Amount in each case as may be specified in the applicable Final Terms. In the case of the USPP Bonds, the Optional Redemption Amount shall be the outstanding nominal amount of the USPP Bond plus the Make-Whole Amount, if any.

In the case of a partial redemption of Bonds, the Bonds to be redeemed (“**Redeemed Bonds**”) will be selected individually by lot, in the case of Redeemed Bonds represented by definitive Bonds, and in accordance with the rules of Euroclear and/or Clearstream, Luxembourg and/or DTC, in the case of Redeemed Bonds represented by a Global Bond, not more than 30 days prior to the date fixed for redemption (such date of selection being hereinafter called the “**Selection Date**”). In the case of Redeemed Bonds represented by definitive Bonds, a list of the serial numbers of such Redeemed Bonds will be published in accordance with Condition 18 not less than 15 days prior to the date fixed for redemption. The aggregate nominal amount of Redeemed Bonds represented by definitive Bonds or represented by a Global Bond shall in each case bear the same proportion to the aggregate nominal amount of all Redeemed Bonds as the aggregate nominal amount of definitive Bonds outstanding and Bonds outstanding represented by such Global Bond, respectively, bears to the aggregate nominal amount of the Bonds outstanding, in each case on the Selection Date, provided that, such first mentioned amount shall, if necessary, be rounded downwards to the nearest integral multiple of the Specified Denomination and the aggregate nominal amount of Redeemed Bonds represented by a Global Bond shall be equal to the balance of the Redeemed Bonds. No exchange of the relevant Global Bond will be permitted during the period from (and including) the Selection Date to (and including) the date fixed for redemption pursuant to this paragraph (d) and notice to that effect shall be given by the Issuer to the Bondholders in accordance with Condition 18 at least five days prior to the Selection Date.

Where Spens Price is specified in the applicable Final Terms as being the Optional Redemption Amount, the Optional Redemption Amount in respect of each Bond shall be the higher of the following:

- (i) its outstanding nominal amount (adjusted, in the case of Indexation Bonds, for indexation in accordance with Condition 9 (the Index Ratio for this purpose being that applicable pursuant to Condition 9(c)(ii)(B) up to and including the date of redemption); and
- (ii) the price determined to be appropriate by a financial adviser in London (selected by the Issuer and approved by the Bond Trustee) as being the price at which the Gross Redemption Yield (as defined below) on the Bonds on the Reference Date (as defined below) is equal to the Gross Redemption Yield at 3.00 p.m. (London time) on the Reference Date on the Reference Gilt (as defined below) while that stock is in issue, and thereafter such United Kingdom government stock as the Issuer may, with the advice of three persons operating in the gilt-edged market (selected by the Issuer and approved by the Bond Trustee) determine to be appropriate.

For the purposes of sub-paragraph (ii) above, “**Gross Redemption Yield**” means a yield expressed as a percentage and calculated on a basis consistent with the basis indicated by the United Kingdom Debt Management Office publication “*Formulae for Calculating Gilt Prices from Yields*” page 4, Section One, Price/Yield Formulae: “*Conventional Gilts; Double-dated and Undated Gilts with Assumed (or Actual) Redemption on a Quasi-Coupon Date*” (published 8 June 1998); “**Reference Date**” means the date which is two Business Days prior to the despatch of the notice of redemption under this paragraph (d), as the case may be; and “**Reference Gilt**” means the reference gilt specified in the applicable Final Terms.

**(e) Early Redemption Amounts**

For the purpose of paragraphs (b) and (c) above and following an Event of Default (save as may otherwise be provided in these Conditions or the relevant Final Terms), each Bond will be redeemed at its Early Redemption Amount calculated as follows:

- (i) in the case of a Bond (other than a Zero Coupon Bond but including an Instalment Bond and a Partly Paid Bond) with a Final Redemption Amount which is or may be less or greater than the Issue Price or which is payable in a Specified Currency other than that in which the Bond is denominated, at the amount specified in, or determined in the manner specified in, the applicable Final Terms or, if no such amount or manner is so specified in the applicable Final Terms, at its nominal amount (adjusted, in the case of Indexation Bonds, for indexation in accordance with Condition 9 (the Index Ratio for this purpose being that applicable pursuant to Condition 9(c)(ii)(B) up to and including the date of redemption)); or
- (ii) in the case of a Zero Coupon Bond, at an amount (the “**Amortised Face Amount**”) calculated in accordance with the following formula:

$$\text{Early Redemption Amount} = \text{RP} \times (1 + \text{AY})^y$$

where:

“**RP**” means the Reference Price; and

“**AY**” means the Accrual Yield expressed as a decimal; and

“**y**” is a fraction the numerator of which is equal to the number of days (calculated on the basis of a 360-day year consisting of 12 months of 30 days each) from (and including) the Issue Date of the first Tranche of the Bonds to (but excluding) the date fixed for redemption or (as the case may be) the date upon which such Bond becomes due and repayable and the denominator of which is 360,

or on such other calculation basis as may be specified in the applicable Final Terms.

**(f) Instalments**

Instalment Bonds will be redeemed in the Instalment Amounts and on the Instalment Dates. In the case of early redemption, the Early Redemption Amount will be determined pursuant to paragraph (e) above.

**(g) Partly Paid Bonds**

Partly Paid Bonds will be redeemed, whether at maturity, early redemption or otherwise, in accordance with the provisions of this Condition and the applicable Final Terms.

**(h) Purchases**

The Obligors may at any time purchase Bonds (provided that, in the case of definitive Bearer Bonds, all unmatured Receipts, Coupons and Talons appertaining thereto are purchased therewith) at any price in the open market or otherwise provided that the Obligors will not and will not permit any Affiliate to purchase or otherwise acquire, directly or indirectly, any of the outstanding USPP Bonds except pursuant to an offer to purchase made by such Obligor or an Affiliate pro rata to the holders of the USPP Bonds at the time outstanding upon the same terms and conditions to each such holder of the USPP Bonds. Any such offer to the holders of the USPP Bonds shall provide each holder with sufficient information to enable it to make an informed decision with respect to such offer, and shall remain open for at least 30 Business Days. If the holders of more than 25 per cent. of the nominal amount of the USPP Bonds then outstanding accept such offer, the Issuer shall promptly notify the remaining holders of such fact and the expiration date for the acceptance by holders of USPP Bonds of such offer shall be extended by the number of days necessary to give each such remaining holder at least 10 Business Days from its receipt of such notice to accept such offer. If purchases are made by tender, tenders must be available to all Bondholders alike.

**(i) Cancellation**

All Bonds which are redeemed will forthwith be cancelled (together with all unmatured Receipts, Coupons and Talons attached thereto or surrendered therewith at the time of redemption). All Bonds so cancelled and any Bonds purchased and cancelled pursuant to paragraph (h) above (together with all unmatured Receipts, Coupons and Talons cancelled therewith) shall be forwarded to the Principal Paying Agent and cannot be reissued or resold.

**(j) Late payment on Zero Coupon Bonds**

If the amount payable in respect of any Zero Coupon Bond upon redemption of such Zero Coupon Bond pursuant to paragraph (a), (b), (c) or (d) above or upon its becoming due and repayable following an Event



of Default is improperly withheld or refused, the amount due and repayable in respect of such Zero Coupon Bond shall be the amount calculated as provided in paragraph (e)(ii) above as though the references therein to the date fixed for the redemption or the date upon which such Zero Coupon Bond becomes due and payable were replaced by references to the date which is the earlier of:

- (i) the date on which all amounts due in respect of such Zero Coupon Bond have been paid; and
- (ii) five days after the date on which the full amount of the moneys payable in respect of such Zero Coupon Bond has been received by the Principal Paying Agent or the Registrar and notice to that effect has been given to the Bondholders in accordance with Condition 18.

**(k) U.S. Private Placement Holders**

*This Condition 10(k) is applicable only in relation to Bonds which are specified as being USPP Bonds in the applicable Final Terms.*

**(i) Make-Whole Amount Calculation**

The Computing Adviser shall determine the estimated aggregate amount of any Make-Whole Amount required to be paid under the Conditions on the fifth Business Day prior to the relevant Optional Redemption Date or such other date on which any Make-Whole Amount is required to be paid, as the case may be, and shall give written notice thereof to the Issuer on such fifth Business Day, which notice shall set forth in reasonable detail the computation thereof; provided, that the failure of the Computing Adviser to make such determination shall not affect the obligation of the Issuer to pay such Make-Whole Amount when due, and the Computing Adviser shall have no liability to the Issuer or any other holder of USPP Bonds for its failure to make such determination. The Make-Whole Amount calculation formula set forth in such notice shall be binding on the Issuer and all of the holders of USPP Bonds, in the absence of manifest error. Four Business Days prior to the relevant Optional Redemption Date or such other date on which any Make-Whole Amount is required to be paid, as the case may be, the Issuer will furnish to each holder of any USPP Bond being so redeemed a certificate signed by a Director of the Issuer setting forth the estimated Make-Whole Amount in respect of the principal amount of USPP Bonds held by such holder to be redeemed, accompanied by a copy of the written notice by the Computing Adviser described in this Condition 10(k). Two Business Days prior to such redemption, the Issuer shall deliver to each holder of USPP Bonds a certificate of a Director of the Issuer specifying the calculation of such Make-Whole Amount as of the Optional Redemption Date or such other date on which any Make-Whole Amount is required to be paid, as the case may be.

**(ii) Definitions:**

In these Conditions:

“**Called Principal**” means, with respect to any USPP Bond, the nominal amount of such USPP Bond that is to be redeemed pursuant to these Conditions;

“**Computing Adviser**” means, with respect to a redemption of USPP Bonds where the Make-Whole Amount is required to be calculated, a financial adviser in London (selected by the Issuer and approved by the Bond Trustee);

“**Discounted Value**” means, with respect to the Called Principal of any USPP Bond, the amount obtained by discounting all Remaining Scheduled Payments with respect to such Called Principal from their respective scheduled due dates to the Settlement Date with respect to such Called Principal, in accordance with accepted financial practice and at a discount factor (applied on the same periodic basis as that on which interest on the USPP Bonds is payable) equal to the Reinvestment Yield with respect to such Called Principal;

“**Make-Whole Amount**” means, with respect to any USPP Bond, an amount equal to the excess, if any, of the Discounted Value of the Remaining Scheduled Payments with respect to the Called Principal of such USPP Bond over the amount of such Called Principal, provided that the Make-Whole Amount may in no event be less than zero;

“**Person**” means an individual, partnership, corporation, limited liability company, association, trust, unincorporated organisation, or a government or agency or political subdivision thereof;

**“Reinvestment Yield”** means, with respect to the Called Principal of any USPP Bond, the Specified Margin (as specified in the applicable Final Terms) over the yield to maturity implied by (i) the yields reported, as of 10:00 a.m. (New York City time) on the second Business Day preceding the Settlement Date with respect to such Called Principal, on the display designated as “Page 678” on the Dow Jones Market Service (or such other display as may replace Page 678 on the Dow Jones Market Service) for actively traded U.S. Treasury securities having a maturity equal to the Remaining Average Life of such Called Principal as of such Settlement Date, or (ii) if such yields are not reported as of such time or the yields reported as of such time are not ascertainable, the Treasury Constant Maturity Series Yields reported, for the latest day for which such yields have been so reported as of the second Business Day preceding the Settlement Date with respect to such Called Principal, in Federal Reserve Statistical Release H.15 (519) (or any comparable successor publication) for actively traded U.S. Treasury securities having a constant maturity equal to the Remaining Average Life of such Called Principal as of such Settlement Date. Such implied yield will be determined, if necessary, by (a) converting U.S. Treasury bill quotations to bond-equivalent yields in accordance with accepted financial practice and (b) interpolating linearly between (1) the actively traded U.S. Treasury security with the maturity closest to and greater than the Remaining Average Life and (2) the actively traded U.S. Treasury security with the maturity closest to and less than the Remaining Average Life;

**“Remaining Average Life”** means, with respect to any Called Principal, the number of years (calculated to the nearest one-twelfth year) obtained by dividing such Called Principal into the sum of the products obtained by multiplying (a) the principal component of each Remaining Scheduled Payment with respect to such Called Principal by (b) the number of years (calculated to the nearest one-twelfth year) that will elapse between the Settlement Date with respect to such Called Principal and the scheduled due date of such Remaining Scheduled Payment;

**“Remaining Scheduled Payments”** means, with respect to the Called Principal of any USPP Bond, all payments of such Called Principal and interest thereon that would be due after the Settlement Date with respect to such Called Principal if no payment of such Called Principal were made prior to its scheduled due date, provided that if such Settlement Date is not a date on which interest payments are due to be made under the terms of the USPP Bonds, then the amount of the next succeeding scheduled interest payment will be reduced by the amount of interest accrued to such Settlement Date and required to be paid on such Settlement Date pursuant to Condition 10(d) or (k);

**“Settlement Date”** means, with respect to the Called Principal of any USPP Bond, the Optional Redemption Date or any other date on which any Make-Whole Amount is required to be paid, as the case may be; and

**“USPP Bonds”** means those Bonds identified as such in the applicable Final Terms relating to any Class A Bonds or Class B Bonds issued by the Issuer after the Effective Date.

## 11. TAXATION

All payments of principal and interest in respect of the Bonds, Receipts and Coupons by the Issuer and the other Obligors or by any Paying Agent, the Registrar, the Bond Trustee, the Security Trustee or any Financial Guarantor will be made without withholding or deduction for or on account of any present or future taxes or duties of whatever nature imposed or levied by or on behalf of any Tax Jurisdiction unless such withholding or deduction is required by law. In such event, the Issuer or, as the case may be, the other Obligors, or else any Paying Agent, the Registrar, the Bond Trustee, the Security Trustee or the Financial Guarantor shall make such payment after such withholding or deduction has been made and shall account to the relevant authorities for the amount so required to be withheld or deducted. None of the Issuer or the other Obligors, any Paying Agent, the Registrar, the Bond Trustee, the Security Trustee or the relevant Financial Guarantor will be obliged to make any additional payments to the Bondholders, Receiptholders or the Couponholders in respect of such withholding or deduction. Except as otherwise provided in the applicable Final Terms, the Issuer or the other Obligors, any Paying Agent, the Registrar, the Bond Trustee, the Security Trustee or the relevant Financial Guarantor may require holders to provide such certifications and other documents as required by applicable law in order to qualify for exemptions from applicable tax laws.

As used herein:

“**Tax Jurisdiction**” means the United Kingdom or any political subdivision or any authority thereof or therein having power to tax or (in the case of payment by AWS Overseas Holdings) the Cayman Islands or any political subdivision or any authority thereof or therein having power to tax.

## 12. PRESCRIPTION

The Bonds (whether in bearer or registered form), Receipts and Coupons will become void unless presented for payment within a period of 10 years (in the case of principal) and five years (in the case of interest) after the Relevant Date (as defined below) therefor.

There shall not be included in any Coupon sheet issued on exchange of a Talon any Coupon the claim for payment in respect of which would be void pursuant to this Condition or Condition 8(b) or any Talon which would be void pursuant to Condition 8(b).

As used herein, the “**Relevant Date**” means the date on which such payment first becomes due, except that, if the full amount of the moneys payable has not been duly received by the Bond Trustee or the Principal Paying Agent or the Registrar, as the case may be, on or prior to such due date, it means the date on which, the full amount of such moneys having been so received, notice to that effect is duly given to the Bondholders in accordance with Condition 18.

## 13. EVENTS OF DEFAULT

The Events of Default relating to the Bonds are set out in Schedule 7 of the Common Terms Agreement.

Following the notification of an Event of Default, the STID provides for a Standstill Period to commence and for restrictions to apply to all Secured Creditors. *(See Chapter 7, “Financing Structure – Intercreditor Arrangements” for details of the extension and termination of the Standstill and for details of the relevant Instructing Groups permitted to instruct the Security Trustee during a Standstill).* The Common Terms Agreement also contains various Trigger Events that will, if they occur, (amongst other things) permit the Majority Creditors to commission an Independent Review, require AWS to discuss its plans for appropriate remedial action and prevent the AWS Services Financing Group from making further Restricted Payments.

### (a) Events of Default

If any Event of Default (as defined in the Master Definitions Agreement) occurs and is continuing, subject always to the terms of the STID, the Bond Trustee may at any time (in accordance with the provisions of the Bond Trust Deed and the STID), having certified in writing that in its opinion the happening of such event is materially prejudicial to the interests of the Bondholders and shall upon the Bond Trustee being so directed or requested, (i) by an Extraordinary Resolution (as defined in the Bond Trust Deed) of holders of the relevant Series of Class A Bonds or, if there are no Class A Bonds outstanding, the Class B Bonds or (ii) in writing by holders of at least one quarter in outstanding nominal amount of the relevant Series of Class A Bonds, or if there are no Class A Bonds outstanding, the Class B Bonds and subject, in each case, to being indemnified and/or secured to its satisfaction, give notice to the Issuer and the Security Trustee that the Bonds of the relevant Series are, and they shall immediately become, due and repayable, at their respective Early Redemption Amounts plus accrued and unpaid interest thereon.

### (b) Confirmation of no Event of Default

The Issuer shall provide written confirmation to the Bond Trustee, on an annual basis, that no Event of Default or other matter which is required to be brought to the Bond Trustee’s attention pursuant to the terms of the Finance Documents has occurred.

### (c) Enforcement of Security

If the Bond Trustee gives written notice to the Issuer and the Security Trustee that an Event of Default has occurred under the Bonds of any Series, a Standstill Period shall commence. The Security Trustee may only enforce the Security acting on the instructions of the Majority Creditors.

### (d) Automatic Acceleration

In the event of the acceleration of the Secured Liabilities (other than a Permitted Acceleration as set out in the STID), the Bonds of each Series shall automatically become due and repayable at their respective

Early Redemption Amounts plus accrued and unpaid interest thereon or as specified in the applicable Final Terms.

**14. RECOURSE AGAINST ISSUER**

No Bondholder, Receiptholder or Couponholder is entitled to take any action against the Issuer or, in the case of holders of Class A Wrapped Bonds, against any Financial Guarantor or against any assets of the Issuer or any Financial Guarantor to enforce its rights in respect of the Bonds or to enforce any of the Security or to enforce any Bond Policy unless the Bond Trustee or the Security Trustee (as applicable), having become bound so to proceed, fails or neglects to do so within a reasonable period and such failure or neglect is continuing.

**15. REPLACEMENT OF BONDS, RECEIPTS, COUPONS AND TALONS**

Should any Bond, Receipt, Coupon or Talon be lost, stolen, mutilated, defaced or destroyed, it may be replaced subject to applicable terms and stock exchange requirements at the specified office of the Principal Paying Agent (in the case of Bearer Bonds, Receipts or Coupons) or the Registrar (in the case of Registered Bonds) upon payment by the claimant of such costs and expenses as may be incurred in connection therewith and on such terms as to evidence and indemnity as the Issuer may require. Mutilated or defaced Bonds, Receipts, Coupons or Talons must be surrendered before replacements will be issued.

**16. AGENTS**

The names of the initial Agents and their initial specified offices are set out below.

The Issuer is entitled (with the prior written approval of the Bond Trustee) to vary or terminate the appointment of any Agent and/or appoint additional or other Agents and/or approve any change in the specified office through which any Agent acts, provided that:

- (a) there will at all times be a Principal Paying Agent and a Registrar;
- (b) so long as the Bonds are listed on any stock exchange or admitted to listing by any other relevant authority, there will at all times be a Paying Agent (in the case of Bearer Bonds) and a Transfer Agent (in the case of Registered Bonds) with a specified office in such place as may be required by the rules and regulations of the relevant stock exchange or, as the case may be, other relevant authority;
- (c) so long as any of the Registered Global Bonds payable in a Specified Currency other than U.S. dollars are held through DTC or its nominee, there will at all times be an Exchange Agent with a specified office in New York City; and
- (d) the Issuer will ensure that it maintains a Paying Agent in a Member State of the European Union that will not be obliged to withhold or deduct tax from payments made under the Bonds pursuant to European Council Directive 2003/48/EC or any other European Union Directive on the taxation of savings income or law implementing or complying with, or introduced in order to conform to, such Directive.

In addition, the Issuer shall forthwith appoint a Paying Agent having a specified office in New York City in the circumstances described in Condition 8(e). Any variation, termination, appointment or change shall only take effect (other than in the case of insolvency, when it shall be of immediate effect) after not less than 30 nor more than 45 days' prior notice thereof shall have been given to the Bondholders in accordance with Condition 18.

In acting under the Agency Agreement, the Agents act solely as agents of the Issuer and the other Obligor and, in certain circumstances specified therein, of the Bond Trustee and do not assume any obligation to, or relationship of agency or trust with, any Bondholders, Receiptholders or Couponholders. The Agency Agreement contains provisions permitting any entity into which any Agent is merged or converted or with which it is consolidated or to which it transfers all or substantially all of its assets to become the successor agent.

**17. EXCHANGE OF TALONS**

On and after the Interest Payment Date on which the final Coupon comprised in any Coupon sheet matures, the Talon (if any) forming part of such Coupon sheet may be surrendered at the specified office

of the Principal Paying Agent or any other Paying Agent in exchange for a further Coupon sheet including (if such further Coupon sheet does not include Coupons to (and including) the final date for the payment of interest due in respect of the Bond to which it appertains) a further Talon, subject to the provisions of Condition 12.

## **18. NOTICES**

All notices regarding the Bearer Bonds will be deemed to be validly given if published in a leading English language daily newspaper of general circulation in London. It is expected that such publication will be made in the *Financial Times* in London. The Issuer shall also ensure that notices are duly published in a manner which complies with the rules and regulations of any stock exchange or any other relevant authority on which the Bearer Bonds are for the time being listed or by which they have been admitted to listing. Any such notice will be deemed to have been given on the date of the first publication or, where required to be published in more than one newspaper, on the date of the first publication in all required newspapers. If publication as provided above is not practicable, a notice will be given in such other manner, and will be deemed to have been given on such date, as the Bond Trustee shall approve.

All notices regarding the Registered Bonds will be deemed to be validly given if sent by first class mail or (if posted to an address overseas) by airmail to the holders (or the first named of joint holders) at their respective addresses recorded in the Register and will be deemed to have been given on the fifth day after mailing (or as specified in the applicable Final Terms) and, in addition, for so long as any Registered Bonds are listed on a stock exchange or admitted to listing by any other relevant authority and the rules of that stock exchange or relevant authority so require, such notice will be published in a daily newspaper of general circulation in the place or places required by those rules.

Until such time as any definitive Bonds are issued, there may, so long as any Global Bonds representing the Bonds are held in their entirety on behalf of Euroclear and/or Clearstream, Luxembourg and/or DTC, be substituted for such publication in such newspaper(s) the delivery of the relevant notice to Euroclear and/or Clearstream, Luxembourg and/or DTC for communication by them to the holders of the Bonds and, in addition, for so long as any Bonds are listed on a stock exchange or are admitted to listing by another relevant authority and the rules of that stock exchange or relevant authority so require, such notice will be published in a daily newspaper of general circulation in the place or places required by those rules. Any such notice shall be deemed to have been given to the holders of the Bonds on the seventh day after the day on which the said notice was given to Euroclear and/or Clearstream, Luxembourg and/or DTC.

Notices to be given by any Bondholder shall be in writing and given by lodging the same, together (in the case of any Bond in definitive form) with the relative Bond or Bonds, with the Principal Paying Agent (in the case of Bearer Bonds) or the Registrar (in the case of Registered Bonds). Whilst any of the Bonds are represented by a Global Bond, such notice may be given by any holder of a Bond to the Principal Paying Agent or the Registrar through Euroclear and/or Clearstream, Luxembourg and/or DTC, as the case may be, in such manner as the Principal Paying Agent, the Registrar and Euroclear and/or Clearstream, Luxembourg and/or DTC, as the case may be, may approve for this purpose.

## **19. MEETINGS OF BONDHOLDERS, MODIFICATION, WAIVER AND SUBSTITUTION**

### **(a) Decisions of Majority Creditors**

The STID contains provisions dealing with the manner in which matters affecting the interests of the Secured Creditors (including the Bond Trustee and the Bondholders) will be dealt with. Bondholders will (subject to various Reserved Matters and Entrenched Rights) be bound by the decisions of the Majority Creditors (and additionally in a Default Situation decisions made pursuant to the Emergency Instructions Procedures). (For details see Chapter 7, “*Financing Structure*” – “*Intercreditor Arrangements*”, “*Voting and Control*”, “*Class A Debt Instructing Group*”, “*Class B Debt Instructing Group*”, “*Entrenched Rights*”, “*Reserved Matters*” and “*Emergency Instruction Procedures*”).

In the circumstances which do not relate to Entrenched Rights or Reserved Matters of the Bondholders (as set out in the STID), prior to a Default Situation, the Bond Trustee shall be entitled to vote as the DIG Representative of holders of each Series of Wrapped Bonds (following the occurrence of an FG Event of Default in respect of the Financial Guarantor of those Wrapped Bonds which is continuing) and the Unwrapped Bonds (other than the USPP Bonds) on intercreditor issues (“*Intercreditor Issues*”) but shall not be entitled to convene a meeting of any one or more Series of Bondholders to consider the relevant matter. To the extent that a Default Situation has occurred and is subsisting, the Bond Trustee may vote on

Intercreditor Issues in its absolute discretion or shall vote in accordance with a direction by those holders of such outstanding Class A Bonds (other than USPP Bonds) or, if there are no Class A Bonds outstanding, Class B Bonds (i) by means of an Extraordinary Resolution of the relevant Series of Bonds or (ii) (in respect of a DIG Proposal to terminate Standstill) as requested in writing by the holders of at least one quarter of the Outstanding Principal Amount of the relevant Series of Class A Bonds, or if there are no Class A Bonds outstanding, Class B Bonds. In any case, the Bond Trustee shall not be obliged to vote unless it has been indemnified and/or secured to its satisfaction.

Whilst a Default Situation is subsisting, certain decisions and instructions may be required in a timeframe which does not allow the Bond Trustee to convene Bondholder meetings. To cater for such circumstances, the Intercreditor Arrangements provide for an emergency instruction procedure. The Security Trustee will be required to act upon instructions contained in an emergency notice (an “Emergency Instruction Notice”). An Emergency Instruction Notice must be signed by DIG Representatives (the “EIN Signatories”) representing 66% per cent. or more of the aggregate Outstanding Principal Amount of the Qualifying Class A Debt or following repayment in full of the Class A Debt, the Qualifying Class B Debt after, *inter alia*, excluding the proportion of Qualifying Debt in respect of which the Bond Trustee is the DIG Representative and in respect of which the Bond Trustee has not voted. The Emergency Instruction Notice must specify the emergency action which the Security Trustee is being instructed to take and must certify that, unless such action is taken within the time frame specified in the Emergency Instruction Notice, the interests of the EIN Signatories will be materially prejudiced.

**(b) Meetings of Bondholders, Modification and Waiver**

The Bond Trust Deed contains provisions for convening meetings of the Bondholders to consider any matter affecting their interests, including the modification of the Bonds, the Receipts, the Coupons or any of the provisions of the Bond Trust Deed, (in the case of Class A Wrapped Bonds and Class B Wrapped Bonds) the Bond Policies and any other Finance Document to which the Bond Trustee is a party (subject to the terms of the STID). Any modification may (except in relation to any Entrenched Right or Reserved Matter of the Bond Trustee (as set out in the STID), subject to the terms of the STID, including, in the case of any of the Class A Wrapped Bonds or Class B Wrapped Bonds, to Entrenched Rights or Reserved Matters of any Financial Guarantor (as set out in the STID) and subject to the provisions concerning ratification and/or meetings of particular combinations of Series of Bonds as set out in Condition 20(b) and the Bond Trust Deed), be made if sanctioned by a resolution passed at a meeting of such Bondholders duly convened and held in accordance with the Bond Trust Deed by a majority of not less than three-quarters of the votes cast (an “**Extraordinary Resolution**”) at such meeting. Such a meeting may be convened by the Bond Trustee or the Issuer, and shall be convened by the Issuer upon the request in writing of the relevant Bondholders holding not less than one-tenth in nominal amount of the relevant Bonds for the time being outstanding.

The quorum at any meeting convened to vote on an Extraordinary Resolution will be one or more persons holding or representing not less than 50 per cent. in nominal amount of the relevant Bonds for the time being outstanding or, at any adjourned meeting, one or more persons being or representing Bondholders, whatever the nominal amount of the relevant Bonds held or represented, provided however, that certain matters as set out in paragraph 5 of the Third Schedule to the Bond Trust Deed (the “**Basic Terms Modifications**”) in respect of the holders of any particular Series of Bonds may be sanctioned only by an Extraordinary Resolution passed at a meeting of Bondholders of the relevant Series of Bonds at which one or more persons holding or representing not less than three-quarters or, at any adjourned meeting, one-quarter in nominal amount of the outstanding Bonds form a quorum. Any Extraordinary Resolution duly passed at any such meeting shall be binding on all the relevant Bondholders, Receiptholders and Couponholders whether present or not.

In addition, a resolution in writing signed by or on behalf of all Bondholders who for the time being are entitled to receive notice of a meeting of Bondholders under the Bond Trust Deed will take effect as if it were an Extraordinary Resolution. Such a resolution in writing may be contained in one document or several documents in the same form, each signed by or on behalf of one or more Bondholders.

**(c) Modification, consent and waiver**

As more fully set out in the Bond Trust Deed (and subject to the conditions and qualifications therein), the Bond Trustee may, without the consent of the Bondholders of any Series, concur with the Issuer or any other relevant parties in making (i) any modification of these Conditions, the Bond Trust Deed, any Bond

Policy or any Finance Document which is of a formal, minor or technical nature or is made to correct a manifest error; and (ii) (except as mentioned in the Bond Trust Deed and subject to the terms of the STID) any other modification and granting any consent under or waiver or authorisation of any breach or proposed breach of these Conditions, the Bond Trust Deed, such Bond Policy or any such Finance Document or other document which is, in the opinion of the Bond Trustee, not materially prejudicial to the interests of the Bondholders of that Series. Any such modification, consent, waiver or authorisation shall be binding on the Bondholders of that Series, and the holders of all relevant Receipts and Coupons and, if the Bond Trustee so requires, notice thereof shall be given by the Issuer to the Bondholders of that Series as soon as practicable thereafter.

The Bond Trustee shall be entitled to assume that any such modification, consent, waiver or authorisation is not materially prejudicial to the Bondholders if the Rating Agencies confirm that there will not be any adverse effect thereof on the original issue ratings of the Bonds.

**(d) Substitution of the Issuer**

As more fully set forth in the STID (and subject to the conditions and qualifications therein), the Bond Trustee may also agree with the Issuer, without reference to the Bondholders, to the substitution of another corporation in place of the Issuer as principal debtor in respect of the Bond Trust Deed and the Bonds of all Series and subject to the Class A Wrapped Bonds continuing to carry the unconditional guarantee of the relevant Financial Guarantor.

**20. BOND TRUSTEE PROTECTIONS**

**(a) Trustee considerations**

Subject to the terms of the STID and Condition 20(b), in connection with the exercise, under these Conditions, the Bond Trust Deed, any Bond Policy or any Finance Document, of its rights, powers, trusts, authorities and discretions (including any modification, consent, waiver or authorisation), the Bond Trustee shall have regard to the interests of the holders of the relevant Series of Class A Bonds, or if there are no Class A Bonds outstanding, the Class B Bonds then outstanding provided that, if the Bond Trustee considers, in its sole opinion, that there is a conflict of interest between the holders of one or more Series of Bonds, it shall consider the interests of the holders of the Class A Bonds, or if there are no Class A Bonds outstanding, the Class B Bonds outstanding with the shortest dated maturity and will not have regard to the consequences of such exercise for the holders of other Series of Bonds or for individual Bondholders, resulting from their being for any purpose domiciled or resident in, or otherwise connected with, or subject to the jurisdiction of, any particular territory. The Bond Trustee shall not be entitled to require from the Issuer or any Financial Guarantor, nor shall any Bondholders be entitled to claim from the Issuer, any Financial Guarantor or the Bond Trustee, any indemnification or other payment in respect of any consequence (including any tax consequence) for individual Bondholders of any such exercise.

**(b) Exercise of rights by Bond Trustee**

Except as otherwise provided in these Conditions and the Bond Trust Deed, when exercising any rights, powers, trusts, authorities and discretions relating to or contained in these Conditions or the Bond Trust Deed (other than in determining or in respect of any Entrenched Right or Reserved Matter relating to the Bonds or any other Basic Terms Modification), which affects or relates to any Class A Wrapped Bonds and/or Class B Wrapped Bonds, the Bond Trustee shall only act with the consent of the relevant Financial Guarantor(s) (provided no FG Event of Default has occurred and is continuing) in accordance with the provisions of the Bond Trust Deed and the Bond Trustee shall not be required to have regard to the interests of the Bondholders in relation to the exercise of such rights, powers, trusts, authorities and discretions and shall have no liability to any Bondholders as a consequence of so acting. As a consequence of being required to act only with the consent of the relevant Financial Guarantor(s) in the circumstances referred to in the previous sentence, the Bond Trustee may not, notwithstanding the provisions of these Conditions, be entitled to act on behalf of the holders of any Series of Bonds. Subject as provided in these Conditions and the Bond Trust Deed, the Bond Trustee will exercise its rights under, or in relation to, the Bond Trust Deed, the Conditions or any Bond Policy in accordance with the directions of the relevant Bondholders, but the Bond Trustee shall not be bound as against the Bondholders to take any such action unless it has (i) (a) (in respect of the matters set out in Condition 13 and Condition 19(a) only) been so requested in writing by the holders of at least 25 per cent. in nominal amount of the relevant Series of Bonds outstanding or (b) been so directed by an Extraordinary Resolution and (ii) been indemnified and/or furnished with security to its satisfaction.

**(c) Decisions under STID binding on all Bondholders**

Subject to the provisions of the STID and the Entrenched Rights and Reserved Matters of the Bond Trustee and the Bondholders, decisions of the Majority Creditors and (in a Default Situation) decisions made pursuant to the Emergency Instructions Procedures will bind the Bond Trustee and the Bondholders in all circumstances.

**21. INDEMNIFICATION OF THE BOND TRUSTEE AND SECURITY TRUSTEE**

**(a) Indemnification of the Bond Trustee**

The Bond Trust Deed contains provisions for indemnification of the Bond Trustee, and for its relief from responsibility, including provisions relieving it from taking any action including taking proceedings against the Issuer, any Financial Guarantor and/or any other person unless indemnified and/or secured to its satisfaction. The Bond Trustee or any of its affiliates are entitled to enter into business transactions with the Issuer, any Financial Guarantor, the other Secured Creditors or any of their respective subsidiaries or associated companies without accounting for any profit resulting therefrom.

**(b) Indemnification of the Security Trustee**

Subject to the Entrenched Rights and Reserved Matters of the Security Trustee, the Security Trustee will only be required to take any action under or in relation to, or to enforce or protect the Security, or any other security interest created by a Finance Document, or a document referred to therein, if instructed to act by the Majority Creditors or Secured Creditors (or their representatives) (as appropriate) and if indemnified to its satisfaction.

**(c) Directions, Duties and Liabilities**

Neither the Security Trustee nor the Bond Trustee, in the absence of its own wilful misconduct, gross negligence or fraud, and in all cases when acting as directed by or subject to the agreement of the Majority Creditors or Secured Creditors (or their representatives) (as appropriate), shall in any way be responsible for any loss, costs, damages or expenses or other liability, which may result from the exercise or non-exercise of any consent, waiver, power, trust, authority or discretion vested in the Security Trustee or the Bond Trustee pursuant to the STID, any Finance Document or any Ancillary Document.

**22. FURTHER ISSUES**

The Issuer shall be at liberty from time to time without the consent of the Bondholders, the Receiptholders or the Couponholders to create and issue further bonds having terms and conditions the same as the Bonds or the same in all respects save for the amount and date of the first payment of interest thereon and so that the same shall be consolidated and form a single Series with the outstanding Bonds.

**23. CONTRACTS (RIGHTS OF THIRD PARTIES) ACT 1999**

No rights are conferred on any person under the Contracts (Rights of Third Parties) Act 1999 to enforce any term of this Bond, but this does not affect any right or remedy of any person which exists or is available apart from that Act.

**24. GOVERNING LAW**

The Bond Trust Deed, the Security Agreement, the Common Terms Agreement, the STID, the Agency Agreement, the relevant Bond Policy (if any), the Bonds, the Receipts and the Coupons and any other Finance Documents are governed by, and shall be construed in accordance with, English law.



## CHAPTER 10

### USE OF PROCEEDS

The net proceeds from each issue of Bonds will be on-lent to Anglian Water under the terms of the Issuer/ Anglian Water Loan Agreement as part of the Intercompany Loan Arrangements to be applied by Anglian Water for its general corporate purposes. See Section 7.1, “*Financing Structure – The Anglian Water Services Financing Group*”.

## CHAPTER 11

### REGULATION OF THE WATER AND SEWERAGE INDUSTRY IN ENGLAND AND WALES

#### 11.1 Water and Sewerage Regulation Generally

##### 11.1.1 Background

The current structure of the water and sewerage industry in England and Wales dates from 1989, when the Water Act 1989 was enacted. Before this, there were ten regional public sector Water Authorities supplying water and sewerage services and 29 privately owned statutory water companies, supplying water only. Under the Water Act 1989, the functions of the Water Authorities relating to water supply (except in areas where those functions were carried out through statutory water companies) and sewerage services, together with the majority of the Water Authorities' property, rights and liabilities, were transferred to ten companies appointed as water and sewerage undertakers in England and Wales. The industry is now made up of the 10 water and sewerage companies and 13 water only companies which are all subject to the same regulatory regime (together, the "**Regulated Companies**", but so that, unless otherwise expressly stated, references to a "Regulated Company" in this Chapter 11 are references to that company in its capacity as a water and sewerage undertaker or, as the case may be, a water undertaker). The provisions of the Water Act 1989 are now contained mainly in the consolidating WIA which itself has been substantially amended by the Water Act 2003. References in this section to statutes are to the WIA unless otherwise stated.

##### 11.1.2 Regulatory Framework

The activities of Regulated Companies are principally regulated by the provisions of the WIA and the WRA, as amended by the Water Act, regulations made under the WIA and the conditions of their licences. Under the WIA, the Secretary of State has a duty to ensure that at all times there is an appointee for every area of England and Wales. Appointments may be made by the Secretary of State or, in accordance with a general authorisation given by him, the DGWS. The Water Act received Royal Assent on 20 November 2003 and contains wide-ranging changes to the WIA and the regulatory framework for Regulated Companies in England and Wales.

The economic regulator for water and sewerage is the DGWS who is aided in his duties by Ofwat, a non-ministerial government department, of which he is the head. The DGWS is responsible for, *inter alia*, setting limits on charges and monitoring and enforcing licence obligations. The Water Act provides that the DGWS and Ofwat are to be replaced by the WSRA (see below). Regulated Companies are required by their licences to make an annual return to Ofwat (including accounts and financial information) to enable Ofwat to assess their activities and affairs. The two principal quality regulators are the DWI (the Chief Inspector of Drinking Water is appointed by the Secretary of State for the Environment, Food and Rural Affairs ("**DEFRA**") and the EA. The description given in this document relates to the structure and regulations that apply in England. Although the structures of the water industry is the same in Wales, different regulations sometimes apply. There are different structures and different regulatory frameworks for water and sewerage services in the remainder of the United Kingdom (Scotland and Northern Ireland).

#### 11.2 The DGWS, the WSRA and the Secretary of State

The DGWS is appointed for a fixed term by the Secretary of State. He is independent of government ministers and may only be removed for incapacity or misbehaviour. The present DGWS is Philip Fletcher who was appointed in the summer of 2000 for an initial (but renewable) term of five years. Philip Fletcher's contract has been extended to 31 March 2006, up to the point when the WSRA assumes the DGWS' duties. He replaced Sir Ian Byatt, who had been the DGWS for the previous 11 years. Under the Water Act the DGWS will be replaced by the WSRA which will be a body corporate and will comprise a chairman and at least two other members. The WSRA will take over all functions and duties currently performed by the DGWS with some additions made by the Water Act. References in this Chapter to the powers, functions and duties of the DGWS should be read with this impending replacement in mind. The WSRA is expected to be created and assume the DGWS's powers in 2006.

Each of the Secretary of State and the DGWS has a primary duty under the WIA to exercise and perform his powers and duties under the WIA in the manner he considers best calculated to secure that:

- the functions of Regulated Companies are properly carried out throughout England and Wales; and
- Regulated Companies are able (in particular, by securing reasonable returns on their capital) to finance the proper carrying out of those functions.

The Water Act includes two new primary duties for the WSRA and the Secretary of State. The first is a new primary duty to execute and perform their powers and duties in the manner best calculated to further the consumer objective, which is to protect the interests of consumers wherever appropriate by promoting competition between persons engaged in, or in commercial activities connected with, the provision of water and sewerage services. For the purpose of the consumer objective, the “interests of consumers” requires the WSRA to take into account the interests of all consumers. However, the WSRA must have regard in particular to consumers who are disabled or chronically sick, of pensionable age, with low incomes or residing in rural areas as well as customers of Regulated Companies whose premises are not eligible to be supplied by a licensed water supplier (see 11.10.2). In addition, the Secretary of State and the WSRA have the power, in exercising any function in relation to water, to have regard to any interests of consumers of gas, electricity and telecommunications services that are affected by the carrying out of that function.

The second new primary duty is to secure that the activities authorised by the licence of a licensed water supplier (see 11.10.2) and any statutory functions imposed on it are properly carried out.

Subject to these primary duties, each of the Secretary of State and the DGWS is required to exercise and perform his powers and duties in the manner he considers best calculated to:

- protect the interests of customers (in particular rural customers) in connection with the fixing and recovery of water and drainage charges, and so that there is no undue preference or discrimination in the fixing of those charges;
- protect the interest of customers of Regulated Companies (and companies connected with them) as respects non-regulated activities in particular by ensuring that (i) transactions are carried out at arm’s length; and (ii) in relation to their regulated business, Regulated Companies maintain and present accounts in a suitable form and manner;
- protect the interests of customers in connection with the benefits that could be secured for them by the application of the proceeds of disposal by Regulated Companies of Protected Land; and
- promote economy and efficiency on the part of Regulated Companies.

There is a new additional secondary duty, introduced by the Water Act, for the WSRA and the Secretary of State to contribute to the achievement of sustainable development. There is also a new power for the Secretary of State to issue statutory guidance to the WSRA concerning how the WSRA might contribute to social and environmental policies. There is also a new duty on DEFRA to encourage water conservation and on all public authorities, as defined, to take into account, where relevant, the desirability of conserving water supplied or to be supplied to premises.

## **11.3 Licences**

### **11.3.1 General**

Under the WIA, each Regulated Company holds a licence and is regulated through the conditions of such licence as well as the WIA. Each licence specifies the geographic area served by the company and imposes a number of conditions on the licence holder that relate to limits on charges, information reporting requirements, various codes of practice, and other matters. The main provisions of Anglian Water’s Licence before the proposed modifications are typical of those of other licences. In addition to the conditions regulating price limits (see 11.8, “*Economic Regulation*”, below), Anglian Water’s Licence also contains conditions regulating infrastructure charges and the making of charges schemes, and imposes prohibitions on undue discrimination and undue preference in charging. Other matters covered by conditions in the Licence include: accounts and the provision of accounting information; codes of practice for customers on

disconnection and on leakage; levels of service and service targets; “ring-fencing” of assets and restrictions on disposal of land; asset management plans; the provision of information to the DGWS; and payments to customers for supply interruptions because of drought. The DGWS is responsible for monitoring compliance with licence conditions and, where necessary, enforcing compliance through procedures laid down in the WIA. See 11.4, “*Enforcement Orders*” below.

The Water Act introduces new forms of licences that will be required to be held by new entrants (see 11.10.2 below).

### 11.3.2 Termination of a Licence

There are certain circumstances provided for in the WIA under which a Regulated Company could cease to hold a licence for all or part of its area:

- (1) a Regulated Company could consent to the making of a replacement appointment or variation, which changes its appointed area, in which case the DGWS has the authority to appoint a new licence holder;
- (2) under Condition O of the licence, where the Secretary of State has given the Regulated Company at least 25 years’ notice and that period of notice has expired;
- (3) under the provisions of the Special Administration regime, the Special Administrator may transfer the business and licence to a successor (see 11.5, “*Enforcement Orders*” below); or
- (4) by the granting of an “inset” appointment over part of a Regulated Company’s existing appointed area to another Regulated Company (see below).

Before making an appointment or variation replacing a Regulated Company, the DGWS or the Secretary of State must consider any representations or objections made. In making an appointment or variation replacing a Regulated Company and, where he makes such an appointment or variation, in determining what provision should be made for the fixing by the new Regulated Company of charges, it is the duty of the Secretary of State or the DGWS to ensure, so far as may be consistent with their duties under the WIA, that the interests of the members and creditors of the existing Regulated Company are not unfairly prejudiced as respects the terms on which the new Regulated Company could accept transfers of property, rights and liabilities from the existing Regulated Company.

An “inset” appointment can be granted to a company seeking to provide water and/or sewerage services on a greenfield site, or to a large user of water and/or sewerage services within an existing Regulated Company’s area, or where the incumbent Regulated Company consents to the variation. The threshold for large user insets has been reduced, from 250 to 50 megalitres of water supplied or likely to be supplied to particular premises in any 12 month period, which has increased the number of large users that are able to qualify for inset appointments. The inset mechanism is intended to continue after the new regime for licensing new entrants under the Water Act has been brought in. New entrants can begin the process of applying for a water supply licence (see 11.10.2) from 1 August 2005, with a view to the licence taking effect in December 2005. The new water supply licensing regime is described in more detail at Section 11.10.2 below.

### 11.3.3 Modification of a Licence

Conditions of a licence may be modified in accordance with the procedures laid down in the WIA. Subject to a power of veto by the Secretary of State of certain proposed modifications, the DGWS may modify the conditions in the licence with the consent of the Regulated Company concerned. Before making the modifications, the DGWS must publish the proposed modifications as part of a consultation process, giving third parties the opportunity to make representations and objections which the DGWS must consider.

In the absence of consent, the only means by which the DGWS can secure a modification is following a modification reference to the Competition Commission. A modification reference may also be required in the event of a direction from the Secretary of State to the effect that, *inter alia*, in his view, the modifications should only be made, if at all, following a reference to the Competition Commission.

A modification reference requires the Competition Commission to investigate and report on whether matters specified in the reference operate, or may be expected to operate, against the public interest and, if so, whether the adverse public interest effect of those matters could be remedied or prevented by modification of the conditions of the licence. In determining whether any particular matter operates or may be expected to operate against the public interest, the Competition Commission is to have regard to the matters in relation to which duties are imposed on the Secretary of State and the DGWS.

If there is an adverse finding, the Competition Commission's report will state whether any adverse effects on the public interest could be remedied or prevented by modification of the licence. If the Competition Commission so concludes, the DGWS must then make such modifications to the licence as appear to him necessary to remedy or prevent the adverse effects specified in the report whilst having regard to the modifications specified therein and after giving due notice and consideration to any representations and objections.

If it appears to the Competition Commission that the proposed modifications are not requisite for the purpose of remedying or preventing the adverse effects specified in its report, the Competition Commission has the power to substitute its own modifications which are requisite for the purpose.

The Competition Commission (and the Secretary of State in certain circumstances) now also has the power, among others, to modify the conditions of the licence after an investigation under its merger or market investigation powers under the Enterprise Act if it is concluded that matters investigated in relation to water or sewerage services broadly were anti-competitive or, in certain circumstances, against the public interest.

The above changes introduced by the Water Act came into force on 1 April 2004.

#### **11.3.4 Water Supply**

Each Regulated Company has a general duty as a water undertaker to develop and maintain an efficient and economical system of water supply and to make arrangements in relation to the provision of water supplies within its appointed area. It also has specific supply duties, including duties to supply water for domestic purposes to premises within the appointed area which are connected to a water main and to connect new premises to a water main. In addition, it may be required in certain circumstances to connect premises outside its appointed area to one of its water mains and to supply water to those premises.

Water supplied for domestic purposes or food production purposes, must be wholesome at the time of supply, which entails compliance with the Water Supply (Water Quality) Regulations 2000 (the "**Water Quality Regulations**"). In certain circumstances, the standards set in those regulations may be relaxed. Where standards or relaxed standards are not being met, the Secretary of State is under a duty to take enforcement action against the supplier. However, Regulated Companies may submit undertakings or apply for an authorised departure to the Secretary of State detailing steps designed to secure or facilitate compliance with those standards. The Secretary of State is not required to take enforcement action for breaches of the Water Quality Regulations if satisfied with the undertakings, or if satisfied that the breaches are of a trivial nature, or if general duties preclude taking enforcement action. The Secretary of State has stated that, except in certain circumstances, it is unlikely that enforcement action will be taken against Regulated Companies which are complying with the terms of their undertakings. Under the WIA, it is a criminal offence for a water undertaker to supply water which is unfit for human consumption. Anglian Water was prosecuted for one such event in 2004 which occurred in 2002 in the Northrepps area of Norfolk. It was fined £3,750 for supplying water unfit with an additional £11,106 costs. There have been no further prosecutions to date.

During 2004, 99.95 per cent. of the tests carried out on samples complied with the mandatory national and European standards as set out in the Water Quality Regulations. Since 1988, Anglian Water has implemented an extensive investment programme to ensure compliance with respect to water leaving treatment works. This work has been largely completed and Anglian Water intends to continue work on distribution mains. Each Regulated Company is under a duty to promote the efficient use of water by its customers.

### **11.3.5 Sewerage Services**

Each Regulated Company has a general duty as a sewerage undertaker to provide, improve, extend and maintain a system of public sewers capable of draining its region effectively, and to make provision for the emptying of sewers and for dealing effectively with their contents. It also has specific sewerage duties, including a duty to comply with a sewer requisition provided certain conditions are met, a duty to provide sewers otherwise than by requisition, and a duty to permit private drains and sewers to be connected to its public sewers.

It is a criminal offence for a person to cause or knowingly permit any poisonous, noxious or polluting matter to enter controlled waters (including most rivers and other inland and coastal waters) other than in accordance with the terms of a discharge consent or with some other lawful authority. The principal prosecuting body is the EA, although third parties also have a right of prosecution. Anglian Water was prosecuted in the financial year 2004-05 in respect of 3 pollution incidents and was fined a total of £52,905 with a further £11,307 awarded in costs.

The terms of discharge consents and the assessment of compliance with those terms vary, depending largely on the type of discharge and when the consents were granted. Within the scope of its powers and duties under the WRA, the EA has discretion as to the terms on which discharge consents are granted or existing consents are altered. The disposal of sewage sludge from sewage treatment works is also controlled.

As regards sewerage, consents are in place in respect of substantially all known discharges by Anglian Water of polluting matter. Substantially all of Anglian Water's sewage treatment works are capable of complying with the conditions of their consents.

In the light of a judgment of the Court of Appeal handed down in March 2001, which held that a sewerage undertaker did not have a right to discharge into a canal owned by the British Waterways Board, Anglian Water has agreed to pay the British Waterways Board a lump sum of £501,000 plus £111,000 per annum for the next five years in respect of historic and future discharges into its canals.

### **11.3.6 Service Standards**

Ofwat makes annual assessments of the serviceability of Regulated Companies' water and sewerage assets on the basis of data submitted in companies' annual returns. For 2003-04 Ofwat assessed Anglian Water's water assets for both infrastructure and non-infrastructure to be 'stable'. For 2003-04 Ofwat assessed Anglian Water's sewerage non-infrastructure assets to be 'marginal' which indicates that there are conflicting trends of indicators within the group. For 2003-04 Ofwat assessed Anglian Water's sewerage infrastructure assets to be deteriorating.

In its June return to Ofwat for 2004-05 Anglian Water has claimed that its water serviceability assessments remain at 'stable' for both infrastructure and non-infrastructure assets. As part of the final determination of price limits for 2005-10, Anglian Water has agreed to restore the serviceability of its waste water assets to 'stable' by the end of March 2007/08 and has submitted a plan to Ofwat to demonstrate the actions being taken to achieve this target. This will be assessed by Ofwat using data provided as part of the 2007-08 return. Progress is also being made to restore sewerage non-infrastructure to a 'stable' assessment. Ofwat will make its provisional serviceability assessments for 2004-05 in August 2005.

Regulated Companies are required to report to the DGWS on their performance against certain service standards, particularly service to customers, in respect of their obligations as water undertakers and sewerage undertakers. If they do not meet certain standards under the DGWS' guaranteed standards scheme, they may be required to pay compensation to customers.

Under the Water Act, Regulated Companies will be required from 1 April 2005 to disclose whether or not they link the remuneration of the directors to levels of customer service attained and to give details of how any links affect remuneration.

## **11.4 Enforcement Orders**

The general duties of Regulated Companies as water or sewerage undertakers are enforceable by the Secretary of State or the DGWS or both. The conditions of the licence (and other duties) are enforceable

by the DGWS alone whilst other duties, including those relating to water quality, are enforceable by the Chief Inspector of Drinking Water.

Where the Secretary of State or the DGWS is satisfied that a Regulated Company is contravening, or has contravened and is likely to do so again, its licence or a relevant statutory or other requirement, either the Secretary of State or the DGWS (whichever is the appropriate enforcement authority) must make a final enforcement order to secure compliance with that condition or requirement, save that, where it appears to the Secretary of State or the DGWS more appropriate to make a provisional enforcement order, he may do so. In determining whether a provisional enforcement order should be made, the Secretary of State or DGWS shall have regard to the extent to which any person is likely to sustain loss or damage as a consequence of such breach before a final enforcement order is made. The Secretary of State or the DGWS will confirm a provisional enforcement order if satisfied that the provision made by the order is needed to ensure compliance with the condition or requirement that is in breach.

There are exemptions from the Secretary of State's and the DGWS's duty to make an enforcement order or to confirm a provisional enforcement order:

- where the contraventions were, or the apprehended contraventions are, of a trivial nature;
- where the company has given, and is complying with, an undertaking to secure or facilitate compliance with the condition or requirement in question; or
- where duties in the WIA preclude the making or confirmation of the order.

The Water Act confers powers on the WSRA or the Secretary of State to impose financial penalties on Regulated Companies and the new licensees introduced by the Water Act. The WSRA and the Secretary of State are given the power to fine such a company up to 10 per cent. of its turnover if it fails to comply with its licence conditions, standards of performance or other obligations. The penalty must also be reasonable in all the circumstances. The Water Act also provides for where a new licensee has caused or contributed to a breach of a Regulated Company's licence or caused or contributed to a Regulated Company contravening a statutory or other requirement; or where a Regulated Company has caused or contributed to the breach of a new licensee's licence or caused or contributed to the breach of the latter's contravening a statutory or other requirement. In those cases, the WSRA may impose an appropriate remedy. A Regulated Company may appeal a penalty order to the Court. The Court may cancel or reduce the penalty or extend the time-scale to pay. The requirement to pay the penalty is suspended until the case is determined. A financial penalty may not be imposed under this provision for an infringement if it is more appropriate to proceed under the Competition Act.

The duty and powers of the WSRA and Secretary of State to make an enforcement order for contravention of licence, statutory or other requirements have been extended by the Water Act so that an order can be made where a contravention is likely (whether or not one has previously occurred) as well as where it is occurring.

The powers just mentioned have been conferred on the Secretary of State with effect from 1 April 2005 (and on the WSRA from its inception in Spring 2006).

### **11.5 Special Administration Orders**

The WIA contains provisions enabling the Secretary of State, or the DGWS with the consent of the Secretary of State, to secure the general continuity of water supply and sewerage services. In certain specified circumstances, the Court may, on the application of the Secretary of State or, with his consent, the DGWS, make a Special Administration Order in relation to a Regulated Company and appoint a Special Administrator. These circumstances include:

- where there has been, or is likely to be, a breach by a Regulated Company of its principal duties to supply water or provide sewerage services or of a final or confirmed provisional enforcement order and, in either case, the breach is serious enough to make it inappropriate for the Regulated Company to continue to hold its licence;
- where the Regulated Company is, or is likely to be, unable to pay its debts;
- where, in a case in which the Secretary of State has certified that it would be appropriate, but for Section 25 of the WIA, for him to petition for the winding up of the Regulated Company under

Section 440 of the Companies Act, it would be just and equitable, as mentioned in that section, for the Regulated Company to be wound up if it did not hold a licence; and

- where the Regulated Company is unable or unwilling adequately to participate in arrangements certified by the Secretary of State or the DGWS to be necessary by reason of, or in connection with, the appointment of a new Regulated Company upon termination of the existing Regulated Company's licence.

In addition, on an application being made to Court, whether by the Regulated Company itself or by its directors, creditors or contributories, for the compulsory winding up of the Regulated Company, the Court would not be entitled to make a winding up order; however, if satisfied that it would be appropriate to make such an order if the Regulated Company were not a company holding a licence, the Court shall instead make a Special Administration Order.

During the period beginning with the presentation of the petition for Special Administration and ending with the making of a Special Administration Order or the dismissal of the petition (the “**Special Administration Petition Period**”), the Regulated Company may not be wound up, no steps may be taken to enforce any security except with the leave of the Court, and subject to such terms as the Court may impose, and no other proceedings or other legal process may be commenced or continued against the Regulated Company or its property except with the leave of the Court.

Once a Special Administration Order has been made, any petition presented for the winding up of the company will be dismissed and any receiver appointed, removed. Whilst a Special Administration Order is in force, those restrictions imposed during the Special Administration Petition Period continue with some modification: an administrative receiver can no longer be appointed (with or without the leave of the Court) and, in the case of certain actions which require the Court's leave, the consent of the Special Administrator is acceptable in its place. See 11.7.2, “*Restrictions on the enforcement of security*” below.

A Special Administrator would, if appointed, be charged with managing the affairs, business and property of the Regulated Company: (i) for the achievement of the purposes of the Special Administration Order; and (ii) in such a manner as protects the respective interests of the members and creditors of the Regulated Company. The purposes of the Special Administration Order consist of (i) transferring to one or more different companies, as a going concern, as much of the business of the Regulated Company as is necessary in order to ensure that the functions which have been vested in the Regulated Company by virtue of its licence are properly carried out; and (ii) pending the transfer, the carrying out of those functions. It would therefore not be open to him to accept an offer to purchase the assets on a break-up basis in circumstances where the purchaser would be unable properly to carry out the relevant functions of a Regulated Company.

The transfer would be effected by a transfer scheme that the Special Administrator would put in place on behalf of the existing Regulated Company. The transfer scheme may provide for the transfer of the property, rights and liabilities of the existing Regulated Company to the new Regulated Company(ies) and may also provide for the transfer of the existing Regulated Company's licence (with modifications as set out in the transfer scheme) to the new Regulated Company(ies). The powers of a Special Administrator include, as part of a transfer scheme, the ability to make modifications to the licence of the existing Regulated Company, subject to the approval of the Secretary of State or the DGWS. The Special Administrator would agree the terms of the transfer of the existing Regulated Company's business to the new Regulated Company(ies), on behalf of the existing Regulated Company. The powers of a Special Administrator include power to exercise any right the Regulated Company may have to seek a review by the DGWS of the Regulated Company's charges pursuant to an Interim Determination. To take effect, the transfer scheme must be approved by the Secretary of State or the DGWS. In addition, the Secretary of State and the DGWS may modify a transfer scheme before approving it or at any time afterwards with the consent of the Special Administrator and each new Regulated Company.

The WIA also grants the Secretary of State, with the approval of the Treasury the power: (i) to make appropriate grants or loans to achieve the purposes of the Special Administration Order and to indemnify the Special Administrator against losses or damages sustained in connection with the carrying out of his functions; and (ii) to guarantee the payment of principal or interest and the discharge of any other financial obligations in connection with any borrowings of the Regulated Company subject to a Special Administration Order.



## 11.6 Protected Land

Under the WIA, there is a prohibition on Regulated Companies disposing of any of their Protected Land except with the specific consent of, or in accordance with a general authorisation given by, the Secretary of State. A consent or authorisation may be given on such conditions as the Secretary of State considers appropriate. For the purpose of these provisions, disposal includes the creation of any interest (including leases, licences, mortgages, easements and wayleaves) in or any right over land, and includes the creation of a charge. All land disposals are reported to Ofwat in the annual return.

Protected Land comprises any land, or any interest or right in or over any land, which:

- was transferred to a water and sewerage company (under the provisions of the Water Act 1989) on 1 September 1989, or was held by a water only company at any time during the financial year 1989/90;
- is, or has at any time on or after 1 September 1989, been held by a company for purposes connected with the carrying out of its regulated water or sewerage functions; or
- has been transferred to a company in accordance with a scheme under Schedule 2 to the WIA from another company, in relation to which the land was Protected Land when the transferring company held an appointment as a water or sewerage undertaker.

Unless a specific consent is obtained from the Secretary of State, all disposals of Protected Land must comply with Condition K of the licence. This condition seeks to ensure (i) that, in disposing of Protected Land, the Regulated Company retains sufficient rights and assets to enable a Special Administrator to manage the business, affairs and property of the Regulated Company so that the purposes of the Special Administration Order can be achieved and (ii) that the best price is received from such disposals so as to secure benefits to customers (where such proceeds were not taken into account when price limits were set, they are shared equally as between customers and shareholders). To this end there are certain procedures for and restrictions on the disposal of Protected Land and special rules apply to disposals by auction or formal tender and to disposals to certain associated companies. These include a restriction on the disposal (except with the consent of the DGWS) of Protected Land required for carrying out the Regulated Business. In addition, Ofwat can impose conditions on disposals of Protected Land including those relating to the manner in which the proceeds of a sale are to be used.

Given the purposes of the WIA (in particular of the Special Administration regime and the restrictions on enforcement of security thereunder) and of Condition K of its Licence, Anglian Water would not expect to obtain, and has not obtained, the consent of the Secretary of State or of the DGWS to the creation of any security (including the Security) over its Protected Land neither has it created any security over its Protected Land.

## 11.7 Security

### 11.7.1 Restrictions on the Granting of Security

A Regulated Company's ability to grant security over its assets and the enforcement of such security are restricted by the provisions of the WIA and its licence. For example, all licences (including Anglian Water's Licence) restrict a Regulated Company's ability to dispose of Protected Land in this way (as explained in 11.6, "*Protected Land*" above). Accordingly, a licence restricts a Regulated Company's ability to create a charge or mortgage over Protected Land.

In addition, provisions in a Regulated Company's licence require the Regulated Company at all times:

- (1) to ensure, so far as is reasonably practicable, that if a Special Administration Order were made in respect of it, it would have sufficient rights and assets (other than financial resources) to enable the Special Administrator to manage its affairs, business and property so that the purpose of such an order could be achieved; and
- (2) to act in the manner best calculated to ensure that it has adequate: (i) financial resources and facilities; (ii) management resources, to enable it to carry out its regulated activities; and (in Anglian Water's Licence) (iii) systems of planning and internal control to enable it to secure the carrying out of its licensed activities including the investment programme necessary to fulfil its licence obligations. These requirements must not be dependent upon

the discharge by any other person of any obligation under or arising from any agreement or arrangement under which that other person has agreed to provide any services to the Regulated Company in its capacity as the Regulated Company.

These provisions further limit the ability of Anglian Water to grant security over its assets, in particular assets required for carrying out the Regulated Business, and limit in practice the ability to enforce such security.

In the case of Anglian Water, the substantial majority of Anglian Water's assets by value is tangible property which is either Protected Land and/or assets that are required for carrying out Anglian Water's Regulated Business and cannot therefore be effectively secured. This necessarily affects the ability of Anglian Water to create a floating charge over the whole or substantially the whole of its business. However, in any event, there is no right under the WIA to block the appointment of a Special Administrator equivalent to the right of a holder of a floating charge over the whole or substantially the whole of the business of a non-Regulated Company may have, in certain circumstances, to block the appointment of a conventional Insolvency Act administrator.

### **11.7.2 Restrictions on the Enforcement of Security**

Under the WIA, the enforcement of security given by a Regulated Company in respect of its assets is prohibited unless the person enforcing the security has first given 14 days' notice to both the Secretary of State and the DGWS. If a petition for Special Administration has been presented leave of the Court is required before such security is enforceable or any administrative receiver can be appointed (or, if an administrative receiver has been appointed between the expiry of the required notice period and presentation of the petition, before the administrative receiver can continue to carry out his functions). These restrictions continue once a Special Administration Order is in force with some modification (see 11.5, "*Special Administration Orders*" above).

Once a Special Administrator has been appointed, he would have the power, without requiring the Court's consent, to deal with property charged pursuant to a floating charge as if it were not so charged. When such property is disposed of under this power, the proceeds of the disposal would, however, be treated as if subject to a floating charge which had the same priority as that afforded by the original floating charge.

A disposal by the Special Administrator of any property secured by a fixed charge given by the Regulated Company could be made only under an order of the Court unless the creditor in respect of whom such security is granted otherwise agreed to such disposal. Such an order could be made if, following an application by the Special Administrator, the Court was satisfied that the disposal would be likely to promote one or more of the purposes for which the order was made (although the Special Administrator is subject to the general duty to manage the company in a manner which protects the respective interests of the creditors and members of the Regulated Company). Upon such disposal, the proceeds to which that creditor would be entitled would be determined by reference to the "best price which is reasonably available on a sale which is consistent with the purposes of the Special Administration Order" as opposed to an amount not less than "open market value" which would apply in a conventional administration for a non-Regulated Company under the Insolvency Act.

Within three months of the making of a Special Administration Order or such longer period as the Court may allow, the Special Administrator must send a copy of his proposals for achieving the purposes of the order to, *inter alios*, the Secretary of State, the DGWS and the creditors of the company. The creditors' approval to the Special Administrator's proposal is not required at any specially convened meeting (unlike in the conduct of a conventional administration under the Insolvency Act). The interests of creditors and members in a Special Administration are still capable of being protected since they have the right to apply to the Court if they consider that their interests are being prejudiced. Such an application may be made by the creditors or members by petition for an order on a number of grounds, including either: (i) that the Regulated Company's affairs, business and property are being or have been managed by the Special Administrator in a manner which is unfairly prejudicial to the interests of its creditors or members; or (ii) that any actual or proposed act of the Special Administrator is/or would be so prejudicial. Except as mentioned below, the Court may make such order as it thinks fit, and any order made by the Court may include an order to require the Special Administrator to refrain from doing or continuing an

act about which there has been a complaint. The exception referred to above is that the Court may not make an order which would prejudice or prevent the achievement of the purposes of the Special Administration order.

### **11.7.3 Enforcement of Security over Shares in Anglian Water**

Under the WIA, the enforcement of security over, and the subsequent sale of, directly or indirectly, the shares in a Regulated Company such as Anglian Water would not be subject to the restrictions described above in relation to the security over Anglian Water's business and assets. Notwithstanding this, given the DGWS's general duties under the WIA to exercise and perform his powers and duties, *inter alia*, to ensure that the functions of a Regulated Company are properly carried out, the Issuer anticipates that any intended enforcement either directly or indirectly of the Security or the Security over, and subsequently any planned disposal of, the shares in Anglian Water to a third party purchaser, would require consultation with the DGWS. In addition, depending on the circumstances, the merger control provisions referred to in 11.10.4, "*Competition in the Water Industry – Merger Regime*" below could apply in respect of any such disposal.

## **11.8 Economic Regulation**

### **11.8.1 General**

Economic regulation of the water industry in England and Wales is based on a system of five year price caps imposed on the amounts Regulated Companies can charge to their customers. This is intended to reward companies for efficiency and quality of service to customers. The system was intended generally to allow companies to retain for a period any savings attributable to efficiency, thus creating incentives to make such gains.

### **11.8.2 K Price Limitation Formula**

The main instrument of economic regulation is the price limits set out in the conditions of the licences. These limit increases in a basket of standard charges made by Regulated Companies for water supply and sewerage services. The weighted average charges increase is limited to the sum of the percentage movement in the RPI plus K, an adjustment factor which may be positive, negative or zero. K is a number set by the DGWS for each Regulated Company individually and may be a different number in different years. Certain charges are not included in the price limitation formula but are determined on an individual basis.

### **11.8.3 Price Control**

A small number of mainly large consumption non-domestic customers are charged in accordance either with individual "special" arrangements, or with standard charges which do not fall within the scope of the tariff basket. These include charges for bulk supplies and charges in respect of infrastructure provision and, where these are not in accordance with standard charges, charges for non-domestic supplies of water and the reception, treatment and disposal of trade effluent. Charges for bulk supplies of water are usually determined on an individual basis, as are charges for some larger non-domestic water supplies and some trade effluent. The charging basis for bulk supplies in some cases provides for annual recalculation by reference to the expenditure associated with the supply. In May 2005 Ofwat published its Tariff Structure and Charges Report for 2005-2006, in which it set out its policy on tariff issues and the approach to be taken in assessing and approving Regulated Companies' charge schemes, including its expectation that customers' bills should broadly reflect the cost of the service provided.

### **11.8.4 Periodic Reviews of K**

K factors are currently redetermined every five years. Following the last Periodic Review, new price limits took effect from 1 April 2005 and are set for the five year period from 1 April 2005 to 31 March 2010. During 2005/06 Ofwat intends to consult on the length of future price review periods.

The DGWS published the Final Determination of future water and sewerage charges 2005-10 on 2 December 2004 and these came into effect on 1 April 2005. The DGWS made a statement on 31 January 2001 in which he indicated his general approach to the carrying out of Periodic Reviews (see the Appendix, "*Ofwat Letter*"). The DGWS published a paper in February 2002

which indicated that, and the basis on which, price limits are to be linked to service levels (see “*Linking Service Levels to Prices*”). Ofwat initiated the 2004 Periodic Review of price limits by publishing the consultation paper “Ofwat’s approach to the periodic review 2004” on 15 October 2002. In March 2003, Ofwat published “Setting water and sewerage price limits for 2005-10: framework and approach”. Having considered the Regulated Companies’ final business plans for the period, Ofwat published an overview of them in May 2004. Ofwat has also stated that the aims of the review are to set price limits that provide best value to customers now and in the future. In the review, Ofwat also intends to enable well managed companies to finance delivery of services in line with relevant standards and requirements and provide incentives for companies to improve efficiency and service delivery.

In the Final Determination, the DGWS has sought to set price limits, in line with his stated aims, at a level providing best value to customers now and in the future whilst also enabling well-managed companies to finance delivery of services in line with relevant standards and requirements, and incentivising companies to improve efficiency and service delivery. Specifically for the period 2005-2010, the DGWS concluded that an increase in price limits was essential to maintain and improve service standards. These limits reflect increased costs to water companies, particularly in the following areas:

- (i) increased running costs arising from changes to taxation, pension and energy costs and legislative changes;
- (ii) increased activity required to maintain the asset network and improve security of supply to ensure no deterioration in services;
- (iii) further improvements to drinking water quality and the environment required by Ministers; and
- (iv) significant reductions in sewer flooding.

Across the 23 water companies of England and Wales, average price limits per year, for the review period are 4.2%, approximately one third less than that sought by the companies. Anglian Water’s average annual price limit is 2.4% (a breakdown of Anglian Water’s year-by-year price limits for the review period is provided at Chapter 4: Anglian Water Business Description, above). This is in contrast with an average price limit per year of 4.6% requested by Anglian Water in its Business Plan.

These price limits are intended to enable Anglian Water to maintain a safe and reliable water supply and effective treatment of sewerage whilst also:

- (i) increasing activity to maintain pipes, sewers and treatment works;
- (ii) installing 89,000 optional meters by 2009-10;
- (iii) delivering a number of defined drinking water and environment quality improvements;
- (iv) resolving or mitigating all known problems identified in the Business Plan where overloaded sewers cause flooding inside properties;
- (v) maintaining access to the capital markets to finance delivery of these outputs at reasonable cost.

Anglian Water’s price limits include a 0.1% element added in recognition of the company’s good service.

#### **11.8.5 Interim Determinations of K**

Condition B of a Regulated Company’s licence provides for the DGWS to determine in certain circumstances whether, and if so how, K should be changed between Periodic Reviews. The procedure for Interim Determinations of K can be initiated either by the Regulated Company or by the DGWS. In Anglian Water’s Licence an application for an Interim Determination of K may be made in respect of a Notified Item, a Relevant Change of Circumstance or where there has been a substantial adverse or favourable effect.

A Notified Item is any item formally notified by the DGWS to the Regulated Company as not having been allowed for (either in full or at all) in K, provided that there has been no Periodic Review subsequent to that notification. Notified Items put forward by the DGWS in the determination of price limits for Anglian Water for the period 2005 to 2010 are: (a) the costs and revenues associated with any difference in the number of domestic customers who opt to switch to measured charges from that assumed by the DGWS; (b) any net increase in bad debt and debt collection costs arising from the loss of power to disconnect residential customers for non-payment from 1 April 2000; (c) costs arising as a result of the implementation of the Traffic Management Act 2004; (d) changes in the charges made by the EA for water abstraction and discharges of treated effluent; and (e) changes in taxation on infrastructure expenditure arising from the introduction of International Financial Reporting Standards or any FRS based on FRED 29.

Relevant Changes of Circumstance are defined in the licences. Such changes include: (a) the application to the Regulated Company of any new or changed legal requirement including any legal requirement ceasing to apply, being withdrawn or not being renewed (to the extent that the legal requirement applies to the Regulated Company in its capacity as a water or sewerage undertaker); (b) any difference in value between actual or anticipated proceeds of disposals of Protected Land and those allowed for at the last Periodic Review or Interim Determination; (c) where on a determination of K allowance has been made for taking steps to secure compliance or facilitate compliance with a legal requirement or achieve a service standard and the Regulated Company has failed to take those steps and (i) as a result, failed to spend the full amount which it was assumed would be spent taking into account savings which may have been achieved by prudent management and (ii) the stated purpose has not otherwise been achieved; and (in some licences, including Anglian Water's) (d) movements in construction prices so as to differ from those assumed in the determination.

An Interim Determination takes account of the costs, receipts and savings to be included in the computation of K which are reasonably attributable to the Notified Items or the Relevant Changes of Circumstance in question and are not recoverable by charges outside the K price limitation formula. The amount and timing of the costs, receipts and savings must be appropriate and reasonable for the Regulated Company in all the circumstances and they must exclude: trivial amounts, any costs which would have been avoided by prudent management action, any savings achieved by management action over and above those which would have been achieved by prudent management action, and any amounts previously allowed for in determining K. These costs are then netted off against the receipts and savings to determine the annual cash flows thereof for each year included in the period over which the costs are to be measured ("**Base Cash Flows**").

The conditions of the licences also specify a materiality threshold which must be reached before any adjustment can be made. In relation to certain licences (including that of Anglian Water) this materiality threshold is reached where the sum of the net present values of (i) Base Cash Flows consisting of operating expenditure and/or loss of revenue calculated over 15 years and (ii) other Base Cash Flows calculated over the period to the next Periodic Review, is equal to at least 10 per cent. of the latest reported turnover attributable to the Regulated Company's water and sewerage business. An adjustment to K (which may be up or down) is then calculated on the basis of a formula broadly designed to enable the Regulated Company to recover the additional allowable costs incurred or to be incurred during the period until the start of the first charging year to which the next Periodic Review applies and attributable to the identified Base Cash Flows. The change is then made for the remainder of the period up to the start of that first charging year. Condition B of the licence sets out in detail the step-by-step methodology which the DGWS is required to apply.

In addition, under the Shipwreck Clause, Anglian Water's Licence permits it or the DGWS to request price limits to be reset if its regulated business either: (i) suffers a substantial adverse effect which could not have been avoided by prudent management action; or (ii) enjoys a substantial favourable effect which is fortuitous and not attributable to prudent management action. For this purpose, the financial impact is calculated in the same way as for the materiality threshold above except that the 10 per cent. threshold is replaced by a 20 per cent. threshold. Since the DGWS' open letter of 31 January 2001 to the Managing Directors of Regulated Companies offering to reinsert the clause in their licences, several other Regulated Companies have accepted

the proposed inclusion of a Shipwreck Clause in their licences and the DGWS has modified their licences accordingly.

#### **11.8.6 References to the Competition Commission**

If the DGWS fails within specified periods to make a determination at a Periodic Review or in respect of an Interim Determination or if the Regulated Company disputes his determination, the Regulated Company may require the DGWS to refer the matter to the Competition Commission for determination by it after making an investigation. The Competition Commission must make its determination in accordance with any regulations made by the Secretary of State and with the principles which apply, by virtue of the WIA, in relation to determinations made by the DGWS. The decisions of the Competition Commission are binding on the DGWS. No Regulated Company has chosen to dispute the Final Determination for 2005-10.

#### **11.8.7 Other Restrictions on Charging**

Under the WIA Regulated Companies must charge for water supplied, or sewerage services provided, to dwellings in accordance with a charges scheme which cannot take effect unless approved by the DGWS and must comply with any requirements prescribed by the Secretary of State by regulations. Regulated Companies are prohibited from disconnecting dwellings and certain other premises for non-payment of charges for water supply.

### **11.9 Drinking Water and Environmental Regulation**

#### **Principal United Kingdom Law**

The water industry is subject to numerous regulatory requirements concerning human health and safety and the protection of the environment.

Under the WRA abstractions must be in accordance with a licence granted by the EA. It is a criminal offence to breach the conditions of an abstraction licence. The Water Act amends the abstraction licensing system in England and Wales to ensure the sustainable use of water. A power is given to the EA to amend or revoke abstraction licences in the interests of environmental protection where a licence has not been used for four years. As drafted, no compensation would be available for any loss suffered as a consequence of any such amendment or revocation and the Government has said that it would expect all abstractors to work with the EA to ensure that any environmentally damaging abstractions are replaced with sustainable alternatives before this provision comes into effect. Also included in the Water Act is a provision requiring all new abstraction licences to be time-limited (and the Government has previously indicated that it expects most existing licences to be converted to a time-limited basis over time) and a provision creating a new right to claim damages against the holder of an abstraction licence for loss or damage due to water abstraction.

The EA has carried out the first stage of consultation on its proposals to amend the scheme for charging abstractors in light of the amendments to the abstraction licensing system made by the Water Act. Ofwat has recognised that the new charging scheme has the potential to increase charges to water undertakers and is considering proposals that increases in charges arising out of compensation payments to abstractors (the recovery of which will be the major cause of increases in charges) will be recoverable from customers. In any event, the increase in water abstraction charges is unlikely to have a material effect on the financial position of Anglian Water.

The EA is also currently considering ways to facilitate and manage water rights trading as part of the implementation of the Water Act. At present, licences may be transferred from one abstractor to another subject to approval by the EA but the circumstances in which this is possible are limited. The EA's proposals address the procedural changes brought about by the Water Act's changes to the rights needed to apply for a licence, the need to advertise applications and the requirement to specify land on most licences. The ability to trade water rights without needing to specify land to which they apply is the key change and is expected to foster the creation of a true market in the rights. The EA published its consultation document on the proposals in June 2003 and responses to that consultation in March 2004. Final guidance on water rights trading is expected to be produced later in 2005.

Anglian Water does not expect to engage in significant trading in the water rights market. It would only be likely to trade with a limited number of licence holders, namely other water companies or large industrial abstractors. Instances of such trading would be rare. Furthermore, Anglian Water would not wish to

reduce through long-term trades the licensed quantities of water it would have available for sale to its customers. Consequently, the impact of the new framework for water rights trading on Anglian Water is not likely to be material.

In April 2001 the EA launched the Catchment Abstraction Management Strategies (“CAMS”) process which is a part of the Government’s plans to reform water resources licensing. The EA has divided England and Wales into catchment areas and intends to work through the CAMS process in each catchment area by 2008. This will involve identifying local water resource issues and consulting with stakeholders such as abstractors, conservation organisations and water users. The EA will then formulate a local strategy for each catchment area based upon sustainable use of water resources. The strategy will give details of the water resource availability in the catchment area and will inform the EA’s abstraction licensing policies for that area. CAMS will also be the vehicle for reviewing time-limited abstraction licences and determining whether and on what terms they should be renewed.

If an abstraction licence potentially affects a site designated under the Habitats Regulations it must be reviewed in accordance with those Regulations. The EA has said that it intends to complete Stage 4 of its review under the Habitats Directive, for high priority sites that may be affected by Anglian Water’s abstraction licences, in March 2006. The capital cost of replacing any deployable output lost as a result of the non-renewal revocation or modification of any abstraction licences is likely to be material.

As a result of CAMS and the Habitats Regulations, the EA has indicated that a reduction of up to 40 MI/d for the Anglian region will be required by 2010 and up to 210 MI/d by 2025. The average deployable output of all Anglian Water sourceworks is 1485 MI/d. The modification or revocation of abstraction licences allows for compensation to be paid, which is recoverable through increased abstraction licence charges, as described above. Anglian Water anticipates that reductions not eligible for compensation will be fully allowed for by the DGWS.

The DWI’s principal task is to ensure that water undertakers in England and Wales are fulfilling their statutory requirements under the WIA and the Water Quality Regulations for the supply of wholesome drinking water. The DWI is part of DEFRA and acts as a technical assessor on behalf of the Secretary of State in respect of the quality of drinking water supplies. It carries out annual technical audits of each water company; this includes an assessment (based on information supplied by the company) of the quality of water in each supply zone, arrangements for sampling and analysis, and progress made on achieving compliance with regulatory and EU requirements. It can also take enforcement action in the event that a water undertaker is in contravention of regulatory requirements concerning the “wholesomeness” of water supplies. Court proceedings can be brought by the DWI in the name of the Chief Inspector of Drinking Water for the offence of supplying water “unfit for human consumption”, for example if discoloured or foul tasting water is supplied to customers. During 2004, 99.95 per cent. of the tests carried out on samples from customers’ taps in Anglian Water’s water supply area complied with the mandatory national and European standards of the Water Quality Regulations.

The EA was established under the Environment Act 1995 and is responsible, in England and Wales, for the protection and improvement of the environment. Its duties include the regulation of abstractions from, and discharges to, controlled waters. Controlled waters include coastal waters, territorial waters extending three miles from shore, inland freshwaters and groundwater.

A consent under the WRA is required from the EA for any discharge of trade or sewage effluent or other poisonous, noxious or polluting matter into controlled waters. It is a criminal offence under the WRA to cause or knowingly permit such a discharge, although there is a defence if it is carried out in compliance with a consent. The principal prosecuting body is the EA. Under the WRA, the EA is empowered to take remedial action to deal with actual or potential pollution of controlled waters and may recover the reasonable costs of any works undertaken from any person who caused or knowingly permitted the pollution (and can also require that person to take the remedial action itself). Anglian Water was prosecuted in the financial year 2004-05 in respect of 3 pollution incidents and was fined a total of £52,905 with a further £11,307 awarded in costs.

Sewerage undertakers are responsible under the WIA for regulating discharges of industrial effluent into their sewers. Industrial and trade sources of wastewater to sewer regulated by Anglian Water predominately arise from the food, drink and chemical industries. It consents these discharges to protect its operations and the environment and compliance is enforced on a risk based approach. Where traders fail to meet the consent limits Anglian Water first tries to work with them to resolve the problems.

However if there is incidence of persistent failures or damaging discharges Anglian Water uses enforcement powers to prevent further reoccurrence.

As a result of a decision of the Court of Appeal in March 2001, sewerage undertakers will in future have to negotiate contracts with the owners of certain watercourses in order to be able to discharge treated waste water effluents into such watercourses.

There are separate legislative controls over discharges to water courses from certain environmentally hazardous processes under the Integrated Pollution Prevention and Control (IPPC) regime which was introduced by the Pollution Prevention and Control Act 1999 and is being phased in on an industry sector basis. The aim of the IPPC regime is to protect the environment from the potentially harmful effects of industrial installations and operators will be required to use the best available techniques to reduce environmental damage both during the life of an installation and following its closure. Depending on the type and volume of waste processed, certain water company activities can be subject to IPPC. The application of IPPC to Anglian Water's installations may give rise to material expenditure.

Anglian Water currently beneficially recycles some 86 per cent. of its sewage sludge by using it on agricultural land as a fertiliser and soil conditioner. This is recognised by the EU Government and the EU Commission as the Best Practicable Environmental Option. Sludge is recycled to agricultural land in accordance with the Sludge (Use in Agriculture) Regulations 1989. The Government is currently amending these Regulations, but the Water Industry has already invested for, and is complying with, the forthcoming amendments in advance of the Regulations coming into force. These amendments will give statutory effect to Anglian Water's voluntary agreement with the British Retail Consortium under the Safe Sludge Matrix. The EU Commission is currently considering proposals to amend the 1986 Sludge Directive (86/278/EEC). There may be some tightening of metals and organic limits, in addition to following the UK approach on pathogen standards. However, the use of treated sludge in agriculture is recognised as important by the Commission, and they have a stated objective 'to increase the quantity of sludge that is used on land in a sustainable manner'.

It should be noted that sludge use in agriculture is subject to both market forces and legislation. Anglian Water and the Water Industry are involved in discussions to ensure stakeholders are reassured about the practice as and when needed. Significant changes to markets or legislation could cause Anglian Water to incur material expenditure, but both legislation and markets have been recognised as a potential material change of circumstance by Ofwat.

Energy use in water and sewage treatment processes is one of Anglian Water's biggest environmental impacts as it results in emissions of greenhouse gases. As part of its sustainable development strategy, Anglian Water aims to reduce emissions of greenhouse gases and to obtain more energy from renewable sources. Anglian Water is subject to the Climate Change Levy introduced in April 2001 as part of the Government's strategy for tackling climate change. According to its own estimate, Anglian Water will incur an annual cost of around £2.6 million under the Climate Change Levy.

Part IIA of the Environmental Protection Act 1990 ("EPA 1990"), together with certain implementing regulations and statutory guidance, establishes a legal regime to address the remediation of historically contaminated land. Current and future impacts are dealt with under other pollution control laws. Under the regime the original polluter or any person who is a "knowing permitter" can be required to clean up contamination of land if it is causing, or there is a significant possibility of it causing, significant harm to the environment or to human health or if pollution of controlled waters is being or is likely to be caused. The Water Act will amend Part IIA of the EPA 1990 in relation to water pollution so that it applies only if significant pollution of controlled waters is being caused or there is a significant possibility of such pollution being caused. If the polluter or a knowing permitter cannot be found, the owner or occupier of the land may be held liable whether or not it caused the contamination. Anglian Water has a large landholding and recognises that some of its sites are or may have been contaminated due to historic practices. At present insufficient information is available to enable Anglian Water to quantify any existing exposure, or the likelihood, size or extent of any future exposure that it may have under Part IIA of the Environmental Protection Act 1990. Given the extent of Anglian Water's landholdings and historic site activities, the costs of remediating any contamination of land or water may be material, although the timeframe during which any such costs might be incurred is difficult to predict. Civil liability may also arise (under such heads of claim as nuisance or negligence) where contamination migrates into or on to third party land and/or impacts upon human health, flora or fauna.



In November 2002, the Government introduced the Control of Asbestos at Work Regulations 2002 concerning the management of risks posed by asbestos in non-domestic premises. With effect from May 2004, the Regulations impose a duty on those who own or control commercial premises to carry out detailed assessments for the presence of asbestos, record its condition and proactively manage the associated risks. Asbestos is present at a number of Anglian Water's properties and there is a risk that Anglian Water may incur material expenditure in managing or removing asbestos located at these properties to comply with the new Regulations.

### **Principal EU Law**

The activities of Regulated Companies are affected by the requirements of EU Directives. Principal EU Directives relating to such activities which are currently in force or are proposed are detailed below.

The Water Framework Directive was adopted in 2000. It is intended to rationalise existing EU water legislation in order to provide a framework for the protection of inland and coastal waters from hazardous substances and to promote sustainable water consumption. The Directive was transposed into English and Welsh law by the Water Environment (Water Framework Directive) (England and Wales) Regulations 2003 which came into force on 2 January 2004. It is expected to have a significant impact on Regulated Companies in the longer term. For example, it may result in increased limitations on abstraction licences and discharge consents, which could cause Anglian Water to incur material expenditure. To comply with the Directive, Member States will have to achieve "good" status for all waters by 2015.

In addition to the Water Framework Directive, a new Groundwater Directive has been proposed. It would require Member States of the EU to monitor and assess groundwater quality on the basis of common criteria and to identify and reverse trends in groundwater pollution. If groundwater quality is improved, Regulated Companies may benefit from reduced costs in cleaning abstracted water. However, there is also a possibility that Regulated Companies may have to bear part of the costs of complying with the Directive. As the proposed directive is currently under discussion, it is difficult at present to determine what, if any, the costs and benefits would be to Regulated Companies like Anglian Water.

The Urban Waste Water Treatment Directive ("UWWTD") relates to the collection, treatment and discharge of urban waste water. The UWWTD lays down minimum requirements for the treatment of municipal waste water and for the disposal of sludge and aims to control the discharge of industrial waste waters. Receiving waters are classified according to their "sensitivity" to nutrient enrichment, with "sensitive" waters being subject to more stringent treatment requirements. The European Commission has commenced infraction proceedings against the United Kingdom, alleging that it has failed to implement the UWWTD correctly by inaccurately designating "sensitive" waters. Included amongst these is the Wash. Depending on the outcome of the infraction proceedings, Anglian Water may be required to make material investment in further treatment processes.

In October 2002, the European Commission adopted a proposal for a Directive concerning the quality of bathing water, which is intended to revise the existing Bathing Water Directive (76/160/EEC). The main objective of the proposal is to improve public health protection, while taking account of changes in science and technology and bathing water management since the original Directive was adopted. Key aspects of the proposed Directive include an obligation to meet a much tighter minimum bathing water quality standard than under the existing Directive, rationalisation of the water quality parameters to be monitored, new rules for the frequency of sampling and improved provision of information to the public concerning bathing water quality. The level of investment required to ensure compliance with the new Directive will depend upon the microbiological parameters ultimately adopted. The draft Directive has not been adopted yet.

The EU's Directive on the Quality of Water intended for Human Consumption sets standards for water intended for drinking, food preparation or other domestic purposes is implemented by the Water Quality Regulations which came into force on 1 January 2004.

There are 23 designated shellfish waters in the Anglian region. Although the Shellfish Waters Directive identifies specific standards applicable to such waters, it is EA policy in respect of meeting government shellfish flesh quality objectives that is likely to drive investment in such waters. Improvements have arisen from the investment required by the UWWTD and the Bathing Water Directive. No further investment was supported by regulators in the recent periodic review to determine work to be delivered in the 2005-10 period.

The Habitats Directive and the Birds Directive establish a network of areas protected by designation across Europe called “Natura 2000” to conserve endangered habitats. Anglian Water owns or has an interest in sites which are directly affected by such designations and also conducts operations from sites adjacent to areas which are protected. Once a site is designated, Member States must take steps to avoid the deterioration of habitats and disturbance of species. As outlined above, this will involve a review of any existing abstraction or discharge authorisations likely to impact upon a protected area. A programme of investment was supported in the recent Periodic Review to deliver improvements at sewage treatment works to meet the requirements of this Directive.

In April 2004 a Directive on environmental liability came into effect, which aims to both prevent and restore environmental damage including water pollution, damage to biodiversity and land contamination which causes serious harm to human health. Under the Directive, operators responsible for certain prescribed activities (for example, those which are subject to IPPC) and which cause environmental damage, would, subject to certain defences, be held strictly liable for restoring the damage caused or made to pay for the restoration. All other operators who cause damage to biodiversity by fault or negligence will be under an obligation to repair the damage. Member States have three years to implement it into national law. Although liability under the Directive will not be retrospective, the Directive may well have a significant impact on Regulated Companies whose operations cause damage to the environment and biodiversity.

## **11.10 Competition in the Water Industry**

### **11.10.1 General**

Each Regulated Company effectively holds a geographic monopoly within its appointed area for the provision of water and sewerage services although there is some limited competition. The DGWS has stated that he will use his powers under the Competition Act to investigate and prohibit anti-competitive practices and abuses of a dominant position to ensure a level playing field in the industry.

The current main methods for introducing competition are:

- inset appointments which allow one Regulated Company to replace another as the statutory undertaker for water or sewerage in a specified geographical area within the other Regulated Company’s appointed territory (see 11.3.2 above);
- facilitating developers, or their contractors, to provide new water mains and service pipes instead of asking Regulated Companies to do the work (“self-lay”). The Water Act has introduced a statutory framework for self-lay (see below);
- common carriage – when a water supply licensee supplies water to eligible customers using a Regulated Company’s network. All Regulated Companies have access codes in place but these are being revised in the light of the Water Act which introduces a statutory framework for common carriage. Ofwat Guidance on Access Codes was published in October 2004, and Ofwat has also published a template for access codes to ensure consistency between Regulated Companies. Ofwat has advised that indicative access prices should be published by 31 August 2005, and access codes by 15 September 2005;
- retail – when a water supply licensee purchases water from the existing water undertaker and supplies water to an eligible customer. The Water Act introduces a statutory framework for such licences;
- cross border supplies where a customer in an area adjacent to a neighbouring Regulated Company’s territory can connect to another Regulated Company’s network and receive a supply; and
- private suppliers or private sewers including on-site water and effluent treatment.

### **11.10.2 The Water Act**

The Water Act 2003 contains provisions aimed at increasing the opportunities for competition in the supply of water services to non-household large users. The eligibility threshold for such users

has been set initially at 50 megalitres per year, though there is a mechanism to amend the threshold.

The Act introduces a system to license new water suppliers either under a “retail licence” or a “combined licence”. New entrants can apply for a licence from 1 August 2005 with a view to it taking effect on 1 December 2005. A “retail licence” enables the holder to purchase water from the Regulated Company to supply to its customers through a wholesale agreement with the Regulated Company. Retail services could range from simply contracting with the customer to provide a supply and billing for the supply, to a much wider range of services including water efficiency planning, metering and providing tailored customer services. A “combined licence” is a retail licence with a supplementary authorisation to allow the holder to introduce water into the supply system (“common carriage”) in connection with a supply to customers’ premises in accordance with its retail authorisation. Such a licensee may have its own water sources or it may purchase water from a neighbouring Regulated Company to import into the “local” Regulated Company’s supply system. This introduction must be done through an access agreement with the relevant Regulated Company. Before a combined licence is granted, the Secretary of State must be consulted so that the DWI can give its assessment as to the applicant’s suitability to introduce water into the public supply network. Regulated Companies are excluded from holding a retail or combined licence but an associated company of a Regulated Company may do so.

Before a Regulated Company is required to provide a wholesale supply of water to a licensee in respect of customers in the Regulated Company’s appointed area, certain conditions must be satisfied. Where a request is made for such a wholesale supply, the Regulated Company is under a duty to take steps to enable the supply to be made and to provide that supply in accordance with terms agreed with the supplier or determined by the WSRA, for example, connecting a new customer to the main. However, there are certain circumstances in which the duty on a Regulated Company to supply a licensee does not apply.

Equally there are conditions on which Regulated Companies are required to allow licensees with a combined licence to introduce water to their supply systems. The duty on Regulated Companies to allow licensees to introduce water is limited to where a request is in connection with a specific supply to a customer under the licensee’s retail authorisation. The Regulated Company will also be under this duty where it has agreed (outside the competition provisions in these clauses) to treat a licensee’s water so that it can be introduced into the supply system and, in connection with that introduction, the licensee requests that the Regulated Company permit the licensee to then introduce water into the supply system for the supply of its customers. The Regulated Company who receives a request to introduce water to its supply system must take steps to permit this in accordance with the terms agreed with the licensee or determined by the WSRA. Such steps may include laying a pipe to connect the licensee’s treatment works with the Regulated Company’s supply system. However, there are certain circumstances in which the duty on the Regulated Company to allow the licensee to introduce water to its supply system does not apply.

A licensee may seek a determination from the WSRA as to whether a refusal on the part of the Regulated Company to provide a wholesale supply or to permit water to be introduced was justified. Where the terms cannot be agreed between the Regulated Company for such an arrangement, the WSRA will determine the terms and conditions and, if the licensee agrees, these will form the contract. The charges payable by the licensee under the agreement or determination must be fixed in accordance with the costs principle.

The costs principle is that Regulated Companies are to recover from licensees two elements of cost to the extent that those sums exceed any financial benefits the Regulated Companies receive as a result of the licensee using the system:

- the direct costs of providing any wholesale supply to a licensee or permitting the introduction of water into the supply system; and
- an appropriate amount (the expenses which the Regulated Company would have ordinarily received from its customers if they had not been supplied by the licensee which cannot be reduced or avoided) of qualifying expenses (those incurred in performing statutory functions) together with a reasonable return on that amount.

Under the Water Act it is an offence to use a Regulated Company's system to supply the premises of a customer unless the supply is made by a Regulated Company or a licensee in pursuance of its licence. It is also an offence to introduce water into a Regulated Company's supply system except for the introduction by a licensee in pursuance of its licence or by another Regulated Company under an agreement with the Regulated Company in question or under a bulk supply agreement. The Secretary of State may, however, by statutory instrument grant exemptions to the above offences.

As a result of the framework set out in the Water Act, the purpose of which is broadly to put common carriage on a statutory basis, the proposed industry-wide forum for developing common carriage has been subsumed into a wider process which will develop and implement the new regime.

The Water Act also sets out a statutory framework for self-lay and adoption of water mains and service pipes including the steps to be taken and the agreement that must be entered into by a developer or self-lay organisation proposing to construct water mains or service pipes which are to be vested in the Regulated Company. It provides that the main must be built in accordance with the agreement of the Regulated Company to enable it to be adopted on completion and Regulated Companies may not connect new mains or service pipes to their public networks unless they are adopted in this way. There are certain situations, however, when appeals can be made to the WSRA if the Regulated Company refuses to enter into an adoption agreement on reasonable terms. The Water Act also sets out that the person who enters into the adoption agreement relating to a water main must pay the Regulated Company's reasonable costs of incorporating the water main within its existing water mains network. It also provides for an offset payment to be made by the Regulated Company to the developer or self-lay organisation equivalent to the discounted estimated sum of the water charges for the first twelve years in respect of the premises expected to be connected to the new main.

In addition to the Water Act, Ofwat issued on 25 March 2002 a letter to Regulatory Directors that set out changes designed to improve incentives for companies which seek to generate new revenues through new bulk supplies or competitive initiatives. At present the price-setting methodology at periodic reviews dampens the incentive for such initiatives by effectively giving companies back the revenue lost through losing a customer and taking away the revenue gained through winning a new customer. To remedy this, Ofwat proposes that companies retain the net revenue gains (or losses) relating to new bulk supplies or competitive non-tariff basket activity (i.e. the larger industrial and commercial customers) for five years. To date these proposals have not been implemented.

### **11.10.3 The Competition Act**

The Competition Act came into force in March 2000 and introduces two prohibitions concerning anti-competitive agreements and conduct and powers of investigation and enforcement.

The Chapter I Prohibition prohibits agreements, decisions by associations of undertakings or concerted practices between undertakings which may affect trade within the UK and which have as their object or effect the prevention, restriction or distortion of competition within the UK. The Chapter II Prohibition prohibits the abuse of a dominant position which may affect trade within the UK.

The DGWS has concurrent powers with the Office of Fair Trading to apply and enforce the Competition Act 1998 to deal with anti-competitive agreements or abuses of dominance relating to the water and sewerage sector, including the power to enforce directions to bring an infringement to an end and to impose fines of up to 10 per cent. of AWG's worldwide group-wide turnover for the infringement up to a maximum of three years. Also any arrangement which infringes the Competition Act may be void and unenforceable and may give rise to claims for damages from third parties. A party to an anti-competitive agreement may also be able to seek relief from the other party if it was in a markedly weaker bargaining position than the other party when the contract was made or where the party seeking relief cannot bear significant responsibility for infringement of the Chapter I Prohibition.

The EA consultation document on the facilitation of trading of water abstraction licences referred to in Section 11.9, “*Drinking Water and Environmental Regulation – Principal United Kingdom Law*” above considered the possibility of abuse by licence holders in a dominant position of an area who may seek to buy up all water rights available in that area to prevent competitors acquiring water rights. The EA considered that this potential problem could be dealt with by the EA assessing all trading applications in terms of reasonable need and for consistency with competition principles, and by Ofwat or the OFT as part of their statutory roles. As such it does not represent a change to the legal framework governing competition in the water industry. See also Section 11.9, “*Drinking Water and Environmental Regulation – Principal United Kingdom Law*” above for a description of the proposed changes to the water abstraction licence trading regime.

On 17 August 2001, Anglian Water received a formal notice from Ofwat regarding a complaint made to it under the Competition Act 1998, alleging that Anglian Water or one of its subsidiaries had breached the Competition Act 1998 by concluding agreements for the supply of water at excessively low prices. Ofwat required certain information to be provided to it in this regard. Anglian Water provided information to Ofwat in September and November 2001. On 26 February 2002, Ofwat requested additional information, clarification of the relationship between Anglian Water and H2GO (an AWG Group company which was involved in pursuing inset appointments), and specified that transactions be accounted for separately to identify relevant costs. Anglian Water provided a number of responses to Ofwat throughout 2002 including separate accounting information as part of the annual June Return to Ofwat. In May 2003, Anglian Water received Ofwat’s conclusions to the North Tees enquiry. Ofwat found no breach of the Competition Act 1998 and no breach of Condition E. Nevertheless, Ofwat disagreed with Anglian Water’s cost allocation for two customers and has notified Anglian Water that it intends to make upward adjustments to the revenue Anglian Water receives at the next Periodic Review if Anglian Water does not revise its charges to Ofwat’s satisfaction. Ofwat also proposes to assume that the third customer be treated as non-appointed business. Further to Ofwat’s request, Anglian Water has submitted separate accounting information for the last three financial years.

#### **11.10.4 Merger Regime**

As a result of changes made by the Enterprise Act and the Water Act, the Office of Fair Trading (“**OFT**”) has a duty to refer to the Competition Commission mergers or proposed mergers between two or more water enterprises where the value of the turnover of the water enterprise being taken over, or the value of the turnover of each of the water enterprises belonging to the person making the takeover exceeds £10 million. In determining whether such a matter operates or may be expected to operate against the public interest, the Competition Commission must assess whether the merger prejudices DGWS’s ability to make comparisons between different water companies. If the Competition Commission decides there is a prejudicial outcome (i.e. that the merger has prejudiced, or may be expected to prejudice, the ability of the DGWS to make comparisons), it must decide whether action should be taken to remedy, mitigate or prevent that prejudice and, if so, what action. Remedies may be structural – total or partial prohibition of a proposed merger; total or partial divestiture of a completed acquisition – or behavioural, such as amendments to a Regulated Company’s licence (for instance regarding the provision of information) or a requirement to maintain separate management. In deciding on remedies, the Competition Commission has regard to any relevant customer benefits (in the form of lower prices, higher quality, greater choice or innovation) of the merger under consideration. The Competition Commission takes the final decision on remedial action, and this decision can be appealed to the Competition Appeals Tribunal (“**CAT**”) by any person sufficiently affected by the decision. Depending on the size of the parties involved, such mergers may require notification to the European Commission under the EU merger regime although the Competition Commission may (protecting a national “legitimate interest”) still investigate the effect on the comparator principle.

In cases of an acquisition of a Regulated Company by a company which is not already a Regulated Company or where the special merger water regime does not otherwise apply, general merger control rules apply. These may call for discussion with the Office of Fair Trading (“**OFT**”) as well as Ofwat. The Enterprise Act amended the UK merger regime for such transactions as of 20 June 2002. Now the OFT, as a body corporate replacing the Director

General of Fair Trading, has the power to investigate any merger within the jurisdiction of the United Kingdom merger regime. The OFT must refer the transaction to the Competition Commission for further investigation if the arrangement could be expected to result in a substantial lessening of competition within any market or markets in the UK for goods or services. In its investigations, the OFT will consult with Ofwat. The Secretary of State in certain limited circumstances may also refer a merger to the Competition Commission to investigate whether the arrangement could be expected to operate against the public interest. Depending on the size of the parties involved, such mergers may require notification to the European Commission under the EU's merger regime.

#### **11.10.5 Market Investigation Regime**

The monopoly regime is also amended by the Enterprise Act and replaced with a market investigation regime. Broadly, this enables the DGWS, the OFT and under a reserve power, Ministers to refer similar situations to the Competition Commission. Investigations under this regime will inquire into markets where it appears that competition has been prevented, restricted or distorted by the structure of a market (or any aspect of its structure), the conduct of persons supplying or acquiring goods or services who operate within it, or the conduct of such persons' customers, but where there has been no obvious breach of the prohibitions on anti-competitive agreements or arrangements or abuse of a dominant position under the Competition Act 1998 or Articles 81 or 82 of the EC Treaty. This competition-based test in effect will not differ greatly from current practice. The Competition Commission will also be responsible for remedies (which may include structural break up). However, where there are public interest considerations, the Secretary of State may intervene and may remedy any adverse effects in the public interest.

#### **11.10.6 Other Enterprise Act reforms**

The Enterprise Act includes other measures to reform the UK competition regime. In particular, measures include the ability of consumer groups to bring actions on behalf of a group of consumers (including for damages) in relation to the Chapter I and II Prohibitions contained in the Competition Act 1998. The role currently performed by the Competition Appeal Tribunal is expanded enabling it to hear claims for damages in competition cases brought by harmed parties and judicial review type appeals of merger decisions. Criminal sanctions including the possibility of imprisonment are also introduced to be imposed on individuals who have been involved in certain cartels, and directors involved in breach of competition law may be disqualified.

### **11.11 Customers' Interests**

#### **11.11.1 General**

The DGWS is responsible for protecting the interests of customers. He monitors the performance and level of service of Regulated Companies and the implementation of a "guaranteed standards" scheme in respect of customer care.

#### **11.11.2 Customer Service Committees and Ofwat National Customer Council**

Under the WIA, the DGWS is required to establish regional Customer Service Committees (the "CSCs"). Each of the 10 CSCs has a Chairman and between 10 and 20 members appointed by the DGWS, who are usually from the local area. Meetings of the full CSCs are held in public and take place at least four times a year. CSCs are funded by Ofwat and each has a full-time Secretariat; expert advice is provided by Ofwat staff. CSCs are independent of both the Regulated Companies and the DGWS and have their own statutory duties. The CSCs review all matters relating to the interests of customers and investigate complaints made by customers against companies. CSCs report back to Ofwat with their views and the DGWS aims to meet each CSC annually.

The Ofwat National Customer Council (the "**Council**"), established by the then DGWS in March 1993, represents all water customers at national and European levels and is made up of the 10 chairs of the CSCs. The Council advises the DGWS on the development of policy and represents the interests of customers in Europe. The Council meets at least five times a year and the DGWS attends part of every meeting. On 24 April 2002, "WaterVoice" was adopted as the new name for the Council and the 10 regional CSCs.

The Water Act introduces a new independent Consumer Council for water consumers whose role is to provide information of use to consumers and to promote the interests of all water consumers. This will replace the CSCs and the Council.

### **11.11.3 Guaranteed Standards**

The guaranteed standards scheme is underpinned by regulations made under Sections 38(2) and 95(2) of the WIA, which prescribe standards of performance in connection with water supply and sewerage services in relation to matters such as the keeping of appointments with customers, dealing with enquiries and complaints from customers, giving notice of interruption of supply, installation of meters and flooding from sewers.

If a Regulated Company does not meet any of the prescribed standards, under the guaranteed standards scheme, the customer is entitled to compensation, normally in the region of £20 for domestic customers and £20 or £50 for business customers (although, in the case of sewer flooding, it can be up to £1,000) within 10 working days of the incident. The availability of such compensation is in addition to the availability of any other remedy the customer may have.

## CHAPTER 12

### MODIFICATIONS MADE TO ANGLIAN WATER'S LICENCE

#### 12.1 Ofwat and the Consultation Process

On 9 January 2002, in accordance with the procedure for modifying a Regulated Company's licence with its consent (see Section 11.3.3, "*Regulation of the Water and Sewerage Industry in England and Wales – Modification of a licence*"), Ofwat published the consultation paper "Proposals for the modification of the Conditions of Appointment of Anglian Water Services Ltd". The paper described the proposals for financial restructuring of Anglian Water; explained the process for consideration of those proposals by Ofwat; set out the regulatory issues and requested comments on Ofwat's assessment of those issues; and described the Licence modifications proposed by the DGWS and invited comments on these. The consultation paper sought views on whether the proposed Licence modifications are appropriate and sufficient to protect customers. It also raised two additional issues for consideration. First, the financing of functions and, second, incentives for ongoing efficiency. The paper stated that these issues are similar to those raised in previous Ofwat consultations concerning Dwr Cymru, Mid Kent Water, Portsmouth Water and Southern Water. As regards financing of functions, Ofwat requested views on whether a highly geared, thin equity structure would be sufficiently robust to withstand cost shocks and to enable Anglian Water to carry out and finance its functions as a water and sewerage undertaker. As regards incentives for ongoing efficiency, Ofwat requested views on whether AWG's reduced equity investment would result in significantly weaker incentives for continuing efficiency improvements.

In April 2002, Ofwat produced a position paper on the restructuring proposals put forward by Anglian Water. Ofwat concluded that it would not object to the proposals on condition that:

- Anglian Water implements the proposed licence modifications as discussed between Anglian Water and Ofwat;
- Anglian Water confirms that the rights proposed for bondholders do not impede the Directors' duties under the Water Industry Act 1991;
- Anglian Water obtains an investment-grade issuer credit rating before the transaction is complete; and
- Anglian Water links its management's remuneration to the performance of Anglian Water.

Anglian Water has satisfied each of these conditions (as to the first of which see Section 12.2 below).

#### 12.2 Licence Modifications

The proposed Licence modifications have been made. However, at the time of the consultation the drafting of the Licence modifications as proposed by Ofwat raised a number of issues of interpretation which led Anglian Water to request clarification of, or changes to, the text of the proposed modifications.

In some cases Ofwat agreed to make changes; in other cases it declined to do so, but provided clarification as to how it intends to interpret and apply particular modifications. Anglian Water agreed to give its consent to the proposed modifications subject to the changes agreed with Ofwat being made and in reliance on and subject to Ofwat interpreting and applying the modifications in accordance with the clarification provided by it.

##### 12.2.1 Ring-fencing of the Regulated Business

The DGWS wishes to ensure that Anglian Water's regulated business is ring-fenced and protected from the risks arising from other activities which may be carried out by the AWG Group so that Anglian Water does not, whether through its involvement in those other activities or by its dividend policy, put at risk its ability either to carry out its functions as a water and sewerage undertaker or to finance them. Certain Licence modifications therefore:

- (i) prohibit the transfer of rights or assets from Anglian Water to any associated company, except with the consent of the DGWS and otherwise than in compliance with his directions concerning the valuation of the asset and the treatment of the consideration in Anglian Water's accounts (being such rights or assets as a Special Administrator would require, if a



Special Administration Order were made, to enable him so to manage the affairs, business and property of Anglian Water that the purposes of the order could be achieved);

- (ii) prohibit Anglian Water from giving a guarantee of any liability of any associated company or making any loan to any such company, except with the consent of the DGWS;
- (iii) prohibit Anglian Water from continuing (except in limited circumstances involving a subsidiary of Anglian Water) or incurring any commitment which includes a 'cross-default obligation' (whereby its financial liabilities are increased or accelerated because of the default of any person other than Anglian Water), except with the consent of the DGWS; and
- (iv) require Anglian Water, or any associated company issuing corporate debt on its behalf, to use all reasonable endeavours to ensure that it maintains an issuer credit rating which is an investment grade rating.

It should be noted that the DGWS has confirmed that he would not regard the cross-default obligations and guarantees described in Section 7.7, "*Financing Structure – Security Agreement*" as being in breach of the prohibitions mentioned in paragraphs (ii) and (iii) above and he has confirmed that he would not regard the loans described in Section 7.4, "*Financing Structure - Intercompany Loan Arrangements*" as being in breach of the prohibition mentioned in paragraph (ii) above.

Anglian Water is already required to certify annually to the DGWS that in the opinion of the Anglian Water directors it has adequate financial and management resources. Further modifications relating to such certification will require:

- (v) Anglian Water to submit a statement of the main factors which the directors have taken into account in giving such a certificate and that all contracts entered into with any associated company include all necessary provisions concerning the standard of service to Anglian Water needed for Anglian Water to meet its obligations as a Regulated Company; to inform the DGWS if the Board of Anglian Water believes that any circumstances might mean that its most recent certificate could not be repeated; and to provide a supporting auditor's report.

Further modifications will require:

- (vi) Anglian Water to declare or pay dividends only in accordance with a dividend policy which has been approved by the Board of Anglian Water and which complies with the principles: (1) that dividends will not impair the ability of Anglian Water to finance its regulated business, and (2) that under a system of incentive regulation, dividends would be expected to reward efficiency and the management of economic risk.

The modifications proposed by Ofwat also include modifications relating to transfer pricing and the terms of contracts between Anglian Water and associated companies, and to the interest cover test for Interim Determination purposes, which are not mentioned in the consultation paper.

### **12.2.2 Management and Control of Anglian Water**

Although Anglian Water remains a subsidiary of AWG, it has its own duties as a Regulated Company. A licence modification therefore requires Anglian Water, in conducting the regulated business, to behave as if it were substantially Anglian Water's sole business and Anglian Water were a separate public limited company. Further modifications oblige Anglian Water to have particular regard to the following in the application of this requirement:

- (i) the composition of the Board of Anglian Water should be such that the directors are able to act independently of the parent company or controlling shareholder and exclusively in the interests of Anglian Water;
- (ii) Anglian Water is to ensure that each of its directors discloses, both to Anglian Water and to the DGWS, any conflicts of interest between duties as directors of Anglian Water and other duties;

- (iii) where potential conflicts exist between the interests of Anglian Water as a Regulated Company and those of other companies in the AWG Group, Anglian Water and its directors must ensure that, in acting as directors of Anglian Water, they should have regard exclusively to the interests of Anglian Water as a Regulated Company;
- (iv) no director of Anglian Water should vote on any contract or arrangement in which he has an interest by virtue of other directorships (this should be reflected in Anglian Water's articles of association);
- (v) Anglian Water should inform the DGWS without delay when a new director is appointed or leaves the Board of Anglian Water or any important change in the functions or executive responsibilities of a director occurs; and
- (vi) Anglian Water should have regard, in particular, to the dividend policy adopted by Anglian Water and the implications of the Licence conditions on the dividend policy (see paragraph 12.2.1(vi)), and to the Principles of Good Governance and Code of Best Practice (and any successor document) recognised by the Listing Rules of the Financial Services Authority.

Anglian Water expressed concern to Ofwat that the modifications as proposed:

- could effectively mean that the directors of Anglian Water could be required to act in what the DGWS considers – rather than what they consider – to be the interests of Anglian Water;
- could provide the DGWS with a basis for questioning and intervening in commercial decisions of the directors of Anglian Water;
- could be construed as precluding the directors of Anglian Water from having due regard to the interests of its shareholders (and hence, indirectly, AWG's shareholders); and
- could be construed as prohibiting executive directors of Anglian Water who are also directors of other AWG Group companies from voting on dividend payments by Anglian Water and a wide range of other proposals.

In response to the concern expressed by Anglian Water, Ofwat provided the following clarification and agreed to make the following changes.

Ofwat stated that the modification referred to in 12.2.2(i) above “is concerned with whether or not the constitution of the board [of Anglian Water] is such that it would allow the directors to act exclusively in the interests of [Anglian Water], not whether directors, either individually or collectively, are in fact doing so”. To underline this point, Ofwat agreed to insert the words “are able to” before the word “act” in that paragraph.

Ofwat also stated that, in assessing compliance with the requirement to conduct the Regulated Business as if it were the sole business of Anglian Water and Anglian Water were a separate public limited company: “we may take account, *inter alia*, of the constitution of the board, but we would not need nor wish to try and second guess whether or not the directors were acting in, or in what they thought were, the interests of” Anglian Water. Ofwat further stated that it did not see this requirement “in any way as the regulator re-interpreting the duties of a director under either the Companies Act or common law... nor in [Ofwat's] view should it be construed as precluding a director from having due regard to the interests of an Appointee's shareholders”.

In relation to the modification referred to in paragraph 12.2.2(iv) above, Ofwat stated that: “We are quite clear ... that directors should be allowed to vote on dividends and our concern is principally with contracts or similar arrangements.”

### **12.2.3 Maintenance of Comparisons with other Water and Sewerage Undertakers**

The DGWS considers that the performance of Anglian Water's regulated business should be transparent to regulators, customers and other water companies. Ofwat has stated that it will assess Anglian Water's performance in terms of efficiency and customer service in exactly the same way as for other Regulated Companies. Accordingly, a modification requires Anglian Water to publish such information about its interim and annual financial results as would be required by the Listing

Rules of the Financial Services Authority if Anglian Water's shares were listed on the London Stock Exchange.

Further modifications require that Anglian Water does not make payments to associated companies for services by those companies to Anglian Water which exceed either prices ascertained through market testing (as set out in Regulatory Accounting Guidelines) or, if in the opinion of the DGWS, Anglian Water has demonstrated that market testing is inappropriate, such portion of the associated company's costs as the DGWS may agree (including a reasonable return to the associated company). Also, Anglian Water is required to obtain from any associated company such information about costs in respect of the latter approach as the DGWS may require.

#### **12.2.4 The Role of AWG as the Owner of Anglian Water**

Anglian Water should have the active co-operation of its owner AWG (or any successor) in complying with its Licence and in the proper discharge of its functions as a Regulated Company. The DGWS proposed modifications to require Anglian Water to procure a legally enforceable undertaking from AWG in favour of Anglian Water, in a form specified by the DGWS, to be given not later than 27 August 2002, that AWG (and each of its subsidiaries (other than Anglian Water and its subsidiaries)) will:

- (i) give Anglian Water all such information as may be necessary to enable Anglian Water to comply with its Licence;
- (ii) refrain from any action which would or may cause Anglian Water to breach any of its obligations under the Water Industry Act 1991 or its Licence; and
- (iii) ensure that the Board of Anglian Water contains not less than three independent non-executive directors, who shall be persons of standing with relevant experience and who shall collectively have connections with and knowledge of the areas within which Anglian Water provides water and sewerage services and an understanding of the interests of the customers of Anglian Water and how these can be respected and protected.

Anglian Water must inform the DGWS, immediately in writing, if it becomes aware that the undertaking has ceased to be legally enforceable, or that there has been any breach of its terms. Anglian Water must not, except with the written consent of the DGWS, enter (directly or indirectly) into any contract or arrangement with AWG or any associated company (other than subsidiaries of Anglian Water) at a time when no such undertaking exists or there is an unremedied breach of such undertaking.

#### **12.2.5 Procurement of Services**

Whilst outsourcing of some operational work is commonplace in the water industry, Anglian Water proposed, at the time of its financial restructuring, to contract out, over time, a substantial proportion of its activities. The only other company that has so far outsourced such a significant proportion of its activities is Dwr Cymru (Welsh Water). The DGWS has proposed that similar Licence modifications to those accepted by Dwr Cymru (Welsh Water) are required for Anglian Water.

All Regulated Companies have the same statutory responsibilities for the proper discharge of their functions. The DGWS considers that any contracting-out of the day-to-day operations of Anglian Water's regulated business must not interfere with its continuing responsibilities as a Regulated Company.

The DGWS proposed that the requirements relating to certification of adequacy of financial and management resources (see 12.2.1 above) be extended to cover certification of the sufficiency of Anglian Water's systems of planning and internal control to secure the carrying out of the regulated business including the investment programme necessary to fulfil its Licence obligations. For these purposes, Anglian Water will be required to ensure that those systems for planning and internal control comply with requirements specified by the DGWS in written guidance. The DGWS stated that the guidance on internal planning and control is based on the Combined Code of the Committee on Corporate Governance and of the Turnbull Report: Internal Control – Guidance for Directors on the Combined Code (September 1999).

In addition, these requirements must not be dependent upon the discharge by any other person of any obligation under which that other person has agreed to provide any services to Anglian Water in its capacity as a Regulated Company.

The DGWS stated that such guidance will require the Board of Anglian Water to pay additional attention to the assessment and handling of hazard and risk, when the services in question are being provided by any contractor. Anglian Water will be required to co-operate with its Reporter (an independent consultant, appointed by Anglian Water with the DGWS' approval). The Reporter will review, audit and challenge Anglian Water's systems for planning and internal control and report to Ofwat, the DWI and the EA upon their effectiveness.

The DGWS also considers it important that Anglian Water pursues proper market-testing of whatever services it chooses to outsource. The DGWS inserted a new Licence Condition (designated as F1) concerning procurement of services. The purpose of the Condition is to ensure that Anglian Water achieves effective and fair competitive tendering of whatever services it may decide not to provide for itself in performing its regulated activities. When the Condition came into effect, any service already being performed by a third party (unless the relevant contract was the result of competitive tendering), must have been either put to tender or brought in-house. The Condition requires:

- (i) Anglian Water to submit a Procurement Plan to the DGWS by not later than 31 December 2002;
- (ii) the Procurement Plan to cover at least the three following years, to be subject to an annual audit by Anglian Water's Reporter and to be revised and resubmitted (that is, rolled forward over the following three years) at least every 18 months and the DGWS may require Anglian Water to submit a revised plan at any time;
- (iii) the Procurement Plan must set out how Anglian Water intends to comply with the obligations set out in (iv) – (viii) below;
- (iv) all procurements of services by Anglian Water must comply with the law, especially the Transfer of Undertakings (Protection of Employment) Regulations 1981, the Utilities Contracts Regulations 1996 and the Competition Act 1998;
- (v) Anglian Water's procurement of services to ensure, so far as possible, that no existing contractor has any competitive advantage over prospective contractors;
- (vi) Anglian Water to facilitate the development of a fully competitive market for the provision of outsourced services necessary for the discharge of its functions as a Regulated Company;
- (vii) Anglian Water to demonstrate that it retains full control of its assets and its ability to discharge its functions as a Regulated Company, including on those occasions where a contractor's performance is in breach of its obligations or a change of contractor is required for any reason, and that Anglian Water is able to obtain all such information from its contractors as is necessary to enable Anglian Water to comply with its Licence;
- (viii) the Procurement Plan to include an explanation of the regulated activities to which it relates;
- (ix) the Procurement Plan to include an assessment of the current contestability of the markets to which the plan relates associated with each of Anglian Water's regulated activities;
- (x) the Procurement Plan to include details of the number, mix and type of contracts currently let or proposed to be let under the Procurement Plan;
- (xi) the Procurement Plan to include details of the procurement processes, terms and conditions of contract. These must be supported by an explanation of how Anglian Water intends to ensure it retains proper and effective control over the prospective contractor's operation, in particular in relation to the requirements of drinking water quality, environment protection,

the provision of proper service to its customers and the guidance of its viability and completeness;

- (xii) the Procurement Plan to include details of how Anglian Water will ensure that its assets, which are to be operated by any contractor will be properly maintained to deliver stable or improving serviceability to customers;
- (xiii) Anglian Water's Reporter to submit a report on the Procurement Plan assessing its viability and completeness; and
- (xiv) Anglian Water to submit to the DGWS annually (and at such other times as the DGWS may require) a written report on its procurement activities, including an explanation for any non-compliance with the Procurement Plan and a statement of the measures taken or proposed to remedy any deficiency; the report must be reviewed by Anglian Water's Reporter who will then submit an assessment of the report to the DGWS.

Anglian Water requested changes to make it clear that the proposed modifications do not apply to existing contracts before expiry or renewal. Although not agreeing to Anglian Water's request, Ofwat stated that: "we agree that the conditions should not in principle apply to existing contracts" and that, subject to Ofwat reviewing existing contracts which have not been subject to competitive tender, it "would not consider [Anglian Water] to be in breach of the licence if these contracts remained in place".

Anglian Water also requested changes to the effect that in procuring services it should not be obliged to put out to tender those minor and other excepted contracts which, under existing laws, are exempt from competitive tendering requirements. The administration and cost implications of having to tender competitively all such contracts could well be disproportionate to any benefits for competition. Although not agreeing to Anglian Water's request, Ofwat stated that: "This does not mean that a full procurement process must be gone through for every contract regardless of size".

Paragraph (vii) above could, in practice, constrain the ability of the Security Trustee to take action in respect of contracts over which a Security Interest is purported to be given under the Security Documents.

Anglian Water's strategy on outsourcing has changed since the financial restructuring, such that the company now expects to retain the majority of its core functions in-house. In recognition of this, Ofwat has suspended its requirement for periodic procurement plans and reports, provided that outsourcing remains at current levels.

#### **12.2.6 Control of Operations**

Certain of these modifications, together with others, are intended to ensure that Anglian Water has adequate controls over its operations. The modifications (1) prohibit the delegation or transfer of responsibility for Anglian Water's functions as a Regulated Company to any other person; (2) require that the obligations on the part of Anglian Water to ensure that it has adequate systems of planning and internal control, financial resources and facilities and management resources are not dependent on the discharge by any other person of any contractual obligation; and (3) require Anglian Water in its procurement of services to demonstrate that it retains full control of all its assets and its ability at all times to discharge its functions as a Regulated Company.

The first of these modifications does not make it clear whether contracting out of services is within the prohibition. Ofwat stated: "We are quite clear that the issue at stake is that whilst responsibility for performance of particular activities can be delegated under contract, responsibility for meeting [Anglian Water's] statutory functions as a relevant undertaker cannot and must not be."

Anglian Water expressed concern as to whether it can in practice comply with the strict letter of the second and third of these modifications, since – like a number of other utility undertakers – it is in fact dependent on certain services provided by external contractors. Ofwat, whilst emphasising that Anglian Water as the licence holder must be able to demonstrate that it has the capacity at all times to meet its statutory functions, and that it retains sufficient control over its operations to enable it to deliver uninterrupted service to customers, stated that the modifications "simply

require that Anglian Water be able to demonstrate that they have in place proper systems of planning and control to ensure proper oversight of their outsourced functions.”

The DGWS also proposed a modification to the effect that if Anglian Water were prosecuted for any offence under the WIA or the Water Resources Act 1991 or any regulations made under either Act, which is alleged to have been committed in relation to a function the performance of which has been contracted out, Anglian Water must not raise any defence of due diligence such as under section 70(3)(b) of the WIA solely on the grounds that responsibility for compliance rested with any other person. Ofwat stated, in relation to this modification, that: “We would not consider [Anglian Water] to be in breach of this [modification] unless it sought to rely on a defence which consisted wholly in it having exercised due diligence in the appointment of its contractors”.

## CHAPTER 13

### BOOK-ENTRY CLEARANCE SYSTEMS

The information set out below is subject to any change in or reinterpretation of the rules, regulations and procedures of DTC, Euroclear or Clearstream, Luxembourg (together, the “**Clearing Systems**”) currently in effect. The information in this section concerning the Clearing Systems has been obtained from sources that the Issuer believes to be reliable, but none of the Issuer, the Bond Trustee or any Dealer takes any responsibility for the accuracy thereof. Investors wishing to use the facilities of any of the Clearing Systems are advised to confirm the continued applicability of the rules, regulations and procedures of the relevant Clearing System. None of the Issuer, the Bond Trustee or any Dealer nor any other party to the Agency Agreement will have any responsibility or liability for any aspect of the records relating to, or payments made on account of, beneficial ownership interests in the Bonds held through the facilities of any Clearing System or for maintaining, supervising or reviewing any records relating to such beneficial ownership interests.

#### **Book-entry Systems**

##### *DTC*

DTC has advised the Issuer that it is a limited purpose trust company organised under the New York Banking Law, a “banking organisation” within the meaning of the New York Banking Law, a “**clearing corporation**” within the meaning of the New York Uniform Commercial Code and a “**clearing agency**” registered pursuant to Section 17A of the Exchange Act. DTC holds securities that its participants (“**Participants**”) deposit with DTC. DTC also facilitates the settlement among Participants of securities transactions, such as transfers and pledges, in deposited securities through electronic computerised book-entry changes in Participants’ accounts, thereby eliminating the need for physical movement of securities certificates. Direct Participants (“**Direct Participants**”) include securities brokers and dealers, banks, trust companies, clearing corporations and certain other organisations. DTC is owned by a number of its Direct Participants and by the New York Stock Exchange, Inc., the American Stock Exchange, Inc. and the National Association of Securities Dealers, Inc. Access to the DTC System is also available to others such as securities brokers and dealers, banks and trust companies that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (“**Indirect Participants**”).

Under the rules, regulations and procedures creating and affecting DTC and its operations (the “**Rules**”), DTC makes book-entry transfers of Registered Bonds among Direct Participants on whose behalf it acts with respect to Bonds accepted into DTC’s book-entry settlement system (“**DTC Bonds**”) as described below and receives and transmits distributions of principal and interest on DTC Bonds. The Rules are on file with the U.S. Securities and Exchange Commission. Direct Participants and Indirect Participants with which beneficial owners of DTC Bonds (“**Owners**”) have accounts with respect to the DTC Bonds similarly are required to make book-entry transfers and receive and transmit such payments on behalf of their respective Owners. Accordingly, although Owners who hold DTC Bonds through Direct Participants or Indirect Participants will not possess Registered Bonds, the Rules, by virtue of the requirements described above, provide a mechanism by which Direct Participants will receive payments and will be able to transfer their interest in respect of the DTC Bonds.

Purchases of DTC Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the DTC Bonds on DTC’s records. The ownership interest of each actual purchaser of each DTC Bond (“**Beneficial Owner**”) is in turn to be recorded on the Direct and Indirect Participant’s records. Beneficial Owners will not receive written confirmation from DTC of their purchase, but Beneficial Owners are expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the DTC Bonds are to be accomplished by entries made on the books of Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in DTC Bonds, except in the event that use of the book-entry system for the DTC Bonds is discontinued.

To facilitate subsequent transfers, all DTC Bonds deposited by Participants with DTC are registered in the name of DTC’s partnership nominee, Cede & Co. The deposit of DTC Bonds with DTC and their registration in the name of Cede & Co. effect no change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the DTC Bonds; DTC’s records reflect only the identity of the Direct Participants to whose accounts such DTC Bonds are credited, which may or may not be the Beneficial Owners. The Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

Redemption notices shall be sent to Cede & Co. If less than all of the DTC Bonds within an issue are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

Neither DTC nor Cede & Co. will consent or vote with respect to DTC Bonds. Under its usual procedures, DTC mails an Omnibus Proxy to the Issuer as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts the DTC Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal and interest payments on the DTC Bonds will be made to DTC. DTC's practice is to credit Direct Participants' accounts on the due date for payment in accordance with their respective holdings shown on DTC's records unless DTC has reason to believe that it will not receive payment on the due date. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name", and will be the responsibility of such Participant and not of DTC or the Issuer, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal and interest to DTC is the responsibility of the Issuer, disbursement of such payments to Direct Participants is the responsibility of DTC, and disbursement of such payments to the Beneficial Owners is the responsibility of Direct and Indirect Participants.

Under certain circumstances, including if there is an Event of Default under the Bonds, DTC will exchange the DTC Bonds for definitive Registered Bonds, which it will distribute to its Participants in accordance with their proportionate entitlements and which, if representing interests in a Rule 144A Global Bond, will be legended as set forth in Chapter 15, "*Subscription and Sale and Transfer and Selling Restrictions*".

Since DTC may only act on behalf of Direct Participants, who in turn act on behalf of Indirect Participants, any Owner desiring to pledge DTC Bonds to persons or entities that do not participate in DTC, or otherwise take actions with respect to such DTC Bonds, will be required to withdraw its Registered Bonds from DTC as described below.

#### *Euroclear and Clearstream, Luxembourg*

Euroclear and Clearstream, Luxembourg each holds securities for its customers and facilitates the clearance and settlement of securities transactions by electronic book-entry transfer between their respective accountholders. Euroclear and Clearstream, Luxembourg provide various services including safekeeping, administration, clearance and settlement of internationally traded securities and securities lending and borrowing. Euroclear and Clearstream, Luxembourg also deal with domestic securities markets in several countries through established depository and custodial relationships. Euroclear and Clearstream, Luxembourg have established an electronic bridge between their two systems across which their respective participants may settle trades with each other.

Euroclear and Clearstream, Luxembourg customers are worldwide financial institutions, including underwriters, securities brokers and dealers, banks, trust companies and clearing corporations. Indirect access to Euroclear and Clearstream, Luxembourg is available to other institutions that clear through or maintain a custodial relationship with an accountholder of either system.

#### **Book-entry Ownership of and Payments in Respect of DTC Bonds**

The Issuer may apply to DTC in order to have any Tranche of Bonds represented by a Registered Global Bond accepted in its book-entry settlement system. Upon the issue of any such Registered Global Bond, DTC or its custodian will credit, on its internal book-entry system, the respective nominal amounts of the individual beneficial interests represented by such Registered Global Bond to the accounts of persons who have accounts with DTC. Such accounts initially will be designated by or on behalf of the relevant Dealer. Ownership of beneficial interests in such a Registered Global Bond will be limited to Direct Participants or Indirect Participants, including, in the case of any Regulation S Global Bond, the respective depositories of Euroclear and Clearstream, Luxembourg. Ownership of beneficial interests in a Registered Global Bond accepted by DTC will be shown on, and the transfer of such ownership will be effected only through, records maintained by DTC or its



nominee (with respect to the interests of Direct Participants) and the records of Direct Participants (with respect to interests of Indirect Participants).

Payments in U.S. dollars of principal and interest in respect of a Registered Global Bond accepted by DTC will be made to the order of DTC or its nominee as the registered holder of such Bond. In the case of any payment in a currency other than U.S. dollars, payment will be made to the Exchange Agent on behalf of DTC or its nominee and the Exchange Agent will (in accordance with instructions received by it) remit all or a portion of such payment for credit directly to the beneficial holders of interests in the Registered Global Bond in the currency in which such payment was made and/or cause all or a portion of such payment to be converted into U.S. dollars and credited to the applicable Participants' account.

The Issuer expects DTC to credit accounts of Direct Participants on the applicable payment date in accordance with their respective holdings as shown in the records of DTC unless DTC has reason to believe that it will not receive payment on such payment date. The Issuer also expects that payments by Participants to beneficial owners of Bonds will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers, and will be the responsibility of such Participant and not the responsibility of DTC, the Principal Paying Agent, the Registrar or the Issuer. Payment of principal, premium, if any, and interest, if any, on Bonds to DTC is the responsibility of the Issuer.

### **Transfers of Bonds Represented by Registered Global Bonds**

Transfers of any interests in Bonds represented by a Registered Global Bond within DTC, Euroclear and Clearstream, Luxembourg will be effected in accordance with the customary rules and operating procedures of the relevant clearing system. The laws in some states within the United States require that certain persons take physical delivery of securities in definitive form. Consequently, the ability to transfer Bonds represented by a Registered Global Bond to such persons may depend upon the ability to exchange such Bonds for Bonds in definitive form. Similarly, because DTC can only act on behalf of Direct Participants in the DTC system who in turn act on behalf of Indirect Participants, the ability of a person having an interest in Bonds represented by a Registered Global Bond accepted by DTC to pledge such Bonds to persons or entities that do not participate in the DTC system or otherwise to take action in respect of such Bonds may depend upon the ability to exchange such Bonds for Bonds in definitive form. The ability of any holder of Bonds represented by a Registered Global Bond accepted by DTC to resell, pledge or otherwise transfer such Bonds may be impaired if the proposed transferee of such Bonds is not eligible to hold such Bonds through a Direct or Indirect Participant in the DTC system.

Subject to compliance with the transfer restrictions applicable to the Registered Bonds described in Chapter 15 under "*Subscription and Sale and Transfer and Selling Restrictions*", cross-market transfers between DTC, on the one hand, and directly or indirectly through Clearstream, Luxembourg or Euroclear accountholders, on the other, will be effected by the relevant clearing system in accordance with its rules and through action taken by the Registrar, the Fiscal Agent and any custodian ("**Custodian**") with whom the relevant Registered Global Bonds have been deposited.

On or after the Issue Date for any Series, transfers of Bonds of such Series between accountholders in Clearstream, Luxembourg and Euroclear and transfers of Bonds of such Series between participants in DTC will generally have a settlement date three business days after the trade date (T+3). The customary arrangements for delivery versus payment will apply to such transfers.

Cross-market transfers between accountholders in Clearstream, Luxembourg or Euroclear and DTC participants will need to have an agreed settlement date between the parties to such transfer. Because there is no direct link between DTC, on the one hand, and Clearstream, Luxembourg and Euroclear, on the other, transfers of interests in the relevant Registered Global Bonds will be effected through the Registrar, the Fiscal Agent and the Custodian receiving instructions (and, where appropriate, certification) from the transferor and arranging for delivery of the interests being transferred to the credit of the designated account for the transferee. In the case of cross-market transfers, settlement between Euroclear or Clearstream, Luxembourg accountholders and DTC participants cannot be made on a delivery versus payment basis. The securities will be delivered on a free delivery basis and arrangements for payment must be made separately.

DTC, Clearstream, Luxembourg and Euroclear have each published rules and operating procedures designed to facilitate transfers of beneficial interests in Registered Global Bonds among participants and accountholders of DTC, Clearstream, Luxembourg and Euroclear. However, they are under no obligation to perform or continue to perform such procedures, and such procedures may be discontinued or changed at any

time. None of the Obligors, the Bond Trustee, the Agents or any Dealer will be responsible for any performance by DTC, Clearstream, Luxembourg or Euroclear or their respective direct or indirect participants or accountholders of their respective obligations under the rules and procedures governing their operations and none of them will have any liability for any aspect of the records relating to or payments made on account of beneficial interests in the Bonds represented by Registered Global Bonds or for maintaining, supervising or reviewing any records relating to such beneficial interests.

## CHAPTER 14

### TAXATION

#### 14.1 United Kingdom

The following is a summary of the United Kingdom withholding taxation treatment at the date of this document in relation to payments of principal and interest in respect of the Bonds. These comments do not deal with other United Kingdom tax aspects of acquiring, holding or disposing of Bonds. They relate only to the position of persons who are absolute beneficial owners of the Bonds. Prospective purchasers of Bonds should be aware that the particular terms of issue of any Series of Bonds as specified in the relevant Final Terms may affect the tax treatment of that and other Series of Bonds. This summary as it applies to United Kingdom taxation is based upon United Kingdom law and HM Revenue & Customs practice in effect on the date of this Prospectus and is subject to any change in law or practice that may take effect after such date.

Bondholders who may be liable to taxation in jurisdictions other than the United Kingdom in respect of their acquisition, holding or disposal of Bonds are particularly advised to consult their professional advisers as to whether they are so liable (and if so under the laws of which jurisdictions), since the following comments relate only to certain United Kingdom taxation aspects of payments in respect of the Bonds. In particular, Bondholders should be aware that they may be liable to taxation under the laws of other jurisdictions in relation to payments in respect of the Bonds even if such payments may be made without withholding or deduction for or on account of taxation under the laws of the United Kingdom.

Prospective purchasers who are in any doubt as to their tax position should consult their professional advisers.

##### 14.1.1 Payment of Interest by the Issuer

Interest on Bonds which are and continue to be listed on a recognised stock exchange within the meaning of section 841 of the United Kingdom Income and Corporation Taxes Act 1988 may be paid without withholding or deduction for or on account of United Kingdom income tax (“**United Kingdom withholding tax**”). The London Stock Exchange is such a recognised stock exchange. Under the current HM Revenue & Customs practice, securities will be listed on the London Stock Exchange if they are admitted to the Official List by the United Kingdom Listing Authority and admitted to trading by the London Stock Exchange. United Kingdom withholding tax at the lower rate (currently 20 per cent.) is generally imposed on interest payments on Bonds that are not listed on a recognised stock exchange subject to any available exemptions or reliefs e.g.:

- (i) where the Issuer reasonably believes (and any person by or through whom interest on the Bonds is paid reasonably believes) that the beneficial owner of such interest is a United Kingdom resident company or a non-United Kingdom resident company within the charge to United Kingdom corporation tax as regards the payment of interest at the time the payment is made, provided that HM Revenue & Customs has not given a direction (in circumstances where it has reasonable grounds to believe that it is likely that the beneficial owner does not qualify for gross payment) that the interest should be paid under deduction of United Kingdom withholding tax; or
- (ii) where an applicable double tax treaty provides for a lower rate of United Kingdom withholding tax (or for no tax to be withheld) in relation to a Bondholder, HM Revenue & Customs can issue a notice to the Issuer to pay interest to the Bondholder without deduction of tax (or for interest to be paid with tax deducted at the rate provided for in the relevant double tax treaty).

Bonds may be issued at an issue price of less than 100 per cent. of their principal amount. Any discount element on any such Bond will not be subject to any United Kingdom withholding tax.

Where Bonds are issued with a redemption premium, as opposed to being issued at a discount, then any such element of premium may constitute a payment of interest. Payments of interest are subject to United Kingdom withholding tax as outlined above, subject to any available exemptions or reliefs (for example the exemptions outlined above).

Unless otherwise specified in the applicable Final Terms, if United Kingdom withholding tax is imposed, then the Issuer will not pay any additional amounts. As specified in the Final Terms applicable to the USPP Bonds issued prior to the date of this Prospectus, if withholding tax is imposed, the Issuer is, in certain circumstances, obliged to pay additional amounts.

#### **14.1.2 Provision of Information by United Kingdom Paying and Collecting Agents**

Persons in the United Kingdom (i) paying interest to or receiving interest on behalf of another person who is an individual, or (ii) paying amounts due on redemption of any Bonds which constitute deeply discounted securities as defined in section 430 of the Income Tax (Trading and Other Income) Act 2005 or receiving such amounts on behalf of another person who is an individual may be required to provide certain information (including the name and address of the beneficial owner of the interest) to HM Revenue & Customs regarding the identity of the persons beneficially entitled to the interest and, in certain circumstances, such information may be exchanged with the tax authorities of other jurisdictions, although in relation to amounts payable on redemption of such Bonds HM Revenue & Customs' published practice indicates that HM Revenue & Customs will not exercise its power to require this information where such amounts are paid on or before 5 April 2006.

#### **14.1.3 EU Savings Directive**

The European Union has adopted a Directive regarding the taxation of savings income. The Directive requires Member States to provide to the tax authorities of another Member State details of payments of interest or other similar income paid by a person to or secured for the benefit of an individual in that other Member State, except that Austria, Belgium and Luxembourg will instead impose a withholding system for a transitional period in relation to such payments unless during such period they elect otherwise.

#### **14.1.4 Payments by Financial Guarantor under the Bond Policies**

If the relevant Financial Guarantor makes any payments in respect of scheduled payments of principal and interest on the Class A Wrapped Bonds and/or the Class B Wrapped Bonds (or other amounts due under the Class A Wrapped Bonds and/or the Class B Wrapped Bonds other than the repayment of amounts subscribed for the Class A Wrapped Bonds and/or the Class B Wrapped Bonds) such payments may be subject to United Kingdom withholding tax subject to any available exemptions or reliefs (for example, the exemptions outlined in 15.1.1 above). If United Kingdom withholding tax is imposed, then the relevant Financial Guarantor will not pay any additional amounts under the Bond Policies.

### **14.2 United States Taxation**

TO ENSURE COMPLIANCE WITH TREASURY DEPARTMENT CIRCULAR 230, HOLDERS ARE HEREBY NOTIFIED THAT: (A) ANY DISCUSSION OF FEDERAL TAX ISSUES IN THIS PROSPECTUS IS NOT INTENDED OR WRITTEN TO BE RELIED UPON, AND CANNOT BE RELIED UPON, BY HOLDERS FOR THE PURPOSE OF AVOIDING PENALTIES THAT MAY BE IMPOSED ON HOLDERS UNDER THE INTERNAL REVENUE CODE; (B) SUCH DISCUSSION IS INCLUDED HEREIN BY THE ISSUER IN CONNECTION WITH THE PROMOTION OR MARKETING (WITHIN THE MEANING OF CIRCULAR 230) BY THE ISSUER OF THE TRANSACTIONS OR MATTERS ADDRESSED HEREIN; AND (C) HOLDERS SHOULD SEEK ADVICE BASED ON THEIR PARTICULAR CIRCUMSTANCES FROM AN INDEPENDENT TAX ADVISOR.

*The following is a summary of certain material U.S. federal income tax consequences of the acquisition, ownership and disposition of Bonds by a U.S. Holder (as defined below). This summary does not address the material U.S. federal income tax consequences of every type of Bond which may be issued under the Programme, and the relevant Final Terms will contain additional or modified disclosure concerning the material U.S. federal income tax consequences relevant to such type of Bond as appropriate. This summary deals only with purchasers of Bonds that are U.S. Holders and that will hold the Bonds as capital assets. The discussion does not cover all aspects of U.S. federal income taxation that may be relevant to, or the actual tax effect that any of the matters described herein will have on, the acquisition, ownership or disposition of Bonds by particular investors, and does not address state, local, foreign or other tax laws. In particular, this summary does not discuss all of the tax considerations that may be*

relevant to certain types of investors subject to special treatment under the U.S. federal income tax laws (such as financial institutions, insurance companies, investors liable for the alternative minimum tax, individual retirement accounts and other tax-deferred accounts, tax-exempt organisations, dealers in securities or currencies, investors that will hold the Bonds as part of straddles, hedging transactions or conversion transactions for U.S. federal income tax purposes or investors whose functional currency is not the U.S. Dollar). Moreover, the summary deals only with Bonds with a term of 30 years or less. The U.S. federal income tax consequences of owning Bonds with a longer term will be discussed in the applicable Final Terms.

As used herein, the term “**U.S. Holder**” means a beneficial owner of Bonds that is, for U.S. federal income tax purposes, (i) a citizen or resident of the United States, (ii) a corporation, created or organised under the laws of the United States or any state thereof, (iii) an estate the income of which is subject to U.S. federal income tax without regard to its source or (iv) a trust if a court within the United States is able to exercise primary supervision over the administration of the trust and one or more U.S. persons have the authority to control all substantial decisions of the trust, or the trust has elected to be treated as a domestic trust for U.S. federal income tax purposes.

The U.S. federal income tax treatment of a partner in a partnership that holds Bonds will depend on the status of the partner and the activities of the partnership. Prospective purchasers that are partnerships should consult their tax adviser concerning the U.S. federal income tax consequences to their partners of the acquisition, ownership and disposition of Bonds by the partnership.

The summary is based on the tax laws of the United States including the Internal Revenue Code of 1986, as amended, its legislative history, existing and proposed regulations thereunder, published rulings and court decisions, as well as on the income tax treaty between the United States and the United Kingdom (the “**Treaty**”) all as currently in effect and all subject to change at any time, possibly with retroactive effect.

Bearer Bonds (including Exchangeable Bearer Bonds while in bearer form) are not being offered to U.S. Holders. A U.S. Holder who owns a Bearer Bond may be subject to limitations under United States income tax laws, including the limitations provided in sections 165(j) and 1287(a) of the United States Internal Revenue Code.

**THE SUMMARY OF U.S. FEDERAL INCOME TAX CONSEQUENCES SET OUT BELOW IS FOR GENERAL INFORMATION ONLY. PROSPECTIVE PURCHASERS SHOULD CONSULT THEIR TAX ADVISERS AS TO THE PARTICULAR TAX CONSEQUENCES TO THEM OF OWNING THE BONDS, INCLUDING THEIR ELIGIBILITY FOR THE BENEFITS OF THE TREATY, THE APPLICABILITY AND EFFECT OF STATE, LOCAL, FOREIGN AND OTHER TAX LAWS AND POSSIBLE CHANGES IN TAX LAW.**

## **Payments of Interest**

### *General*

Interest on a Bond, whether payable in U.S. Dollars or a currency, composite currency or basket of currencies other than U.S. Dollars (a “**foreign currency**”), other than interest on a “Discount Bond” that is not “qualified stated interest” (each as defined below under “*Original Issue Discount – General*”), will be taxable to a U.S. Holder as ordinary income at the time it is received or accrued, depending on the holder’s method of accounting for tax purposes. Interest paid by the Issuer on the Bonds and original issue discount (“**OID**”), if any, accrued with respect to the Bonds (as described below under “*Original Issue Discount*”) generally will constitute income from sources outside the United States. A U.S. Holder of a Bond that is not listed on a recognised stock exchange, and is therefore not eligible for exemption from United Kingdom withholding tax, will nonetheless not be subject to United Kingdom withholding tax if the U.S. Holder is eligible for benefits under the Treaty. Prospective purchasers should consult their tax advisers concerning the applicability of the foreign tax credit and the source of income rules to income attributable to the Bonds.

## **Original Issue Discount**

### *General*

The following is a summary of the principal U.S. federal income tax consequences of the ownership of Bonds issued with OID. The following summary does not discuss Bonds that are characterised as

contingent payment debt instruments for U.S. federal income tax purposes. In the event the Issuer issues contingent payment debt instruments the applicable Final Terms will describe the material U.S. federal income tax consequences thereof.

A Bond, other than a Bond with a term of one year or less (a “**Short-Term Bond**”), will be treated as issued with OID (a “**Discount Bond**”) if the excess of the Bond’s “stated redemption price at maturity” over its issue price is equal to or more than a *de minimis* amount (0.25 per cent. of the Bond’s stated redemption price at maturity multiplied by the number of complete years to its maturity). An obligation that provides for the payment of amounts other than qualified stated interest before maturity (an “**instalment obligation**”) will be treated as a Discount Bond if the excess of the Bond’s stated redemption price at maturity over its issue price is greater than 0.25 per cent. of the Bond’s stated redemption price at maturity multiplied by the weighted average maturity of the Bond. A Bond’s weighted average maturity is the sum of the following amounts determined for each payment on a Bond (other than a payment of qualified stated interest): (i) the number of complete years from the issue date until the payment is made multiplied by (ii) a fraction, the numerator of which is the amount of the payment and the denominator of which is the Bond’s stated redemption price at maturity. Generally, the issue price of a Bond will be the first price at which a substantial amount of Bonds included in the issue of which the Bond is a part is sold to persons other than bond houses, brokers, or similar persons or organisations acting in the capacity of underwriters, placement agents, or wholesalers. The stated redemption price at maturity of a Bond is the total of all payments provided by the Bond that are not payments of “qualified stated interest.” A qualified stated interest payment is generally any one of a series of stated interest payments on a Bond that are unconditionally payable at least annually at a single fixed rate (with certain exceptions for lower rates paid during some periods), or a variable rate (in the circumstances described below under “*Variable Interest Rate Bonds*”), applied to the outstanding principal amount of the Bond.

Solely for the purposes of determining whether a Bond has OID, the Issuer will be deemed to exercise any call option that has the effect of decreasing the yield on the Bond, and the U.S. Holder will be deemed to exercise any put option that has the effect of increasing the yield on the Bond.

U.S. Holders of Discount Bonds must include OID in income calculated on a constant-yield method before the receipt of cash attributable to the income, and generally will have to include in income increasingly greater amounts of OID over the life of the Discount Bonds. The amount of OID includible in income by a U.S. Holder of a Discount Bond is the sum of the daily portions of OID with respect to the Discount Bond for each day during the taxable year or portion of the taxable year on which the U.S. Holder holds the Discount Bond (“**accrued OID**”). The daily portion is determined by allocating to each day in any “accrual period” a pro rata portion of the OID allocable to that accrual period. Accrual periods with respect to a Bond may be of any length selected by the U.S. Holder and may vary in length over the term of the Bond as long as (i) no accrual period is longer than one year and (ii) each scheduled payment of interest or principal on the Bond occurs on either the final or first day of an accrual period. The amount of OID allocable to an accrual period equals the excess of (a) the product of the Discount Bond’s adjusted issue price at the beginning of the accrual period and the Discount Bond’s yield to maturity (determined on the basis of compounding at the close of each accrual period and properly adjusted for the length of the accrual period) over (b) the sum of the payments of qualified stated interest on the Bond allocable to the accrual period. The “adjusted issue price” of a Discount Bond at the beginning of any accrual period is the issue price of the Bond increased by (x) the amount of accrued OID for each prior accrual period and decreased by (y) the amount of any payments previously made on the Bond that were not qualified stated interest payments.

#### *Acquisition Premium*

A U.S. Holder that purchases a Discount Bond for an amount less than or equal to the sum of all amounts payable on the Bond after the purchase date, other than payments of qualified stated interest, but in excess of its adjusted issue price (any such excess being “**acquisition premium**”) and that does not make the election described below under “*Election to Treat All Interest as Original Issue Discount*”, is permitted to reduce the daily portions of OID by a fraction, the numerator of which is the excess of the U.S. Holder’s adjusted basis in the Bond immediately after its purchase over the Bond’s adjusted issue price, and the denominator of which is the excess of the sum of all amounts payable on the Bond after the purchase date, other than payments of qualified stated interest, over the Bond’s adjusted issue price.

### *Market Discount*

A Bond, other than a Short-Term Bond, generally will be treated as purchased at a market discount (a “**Market Discount Bond**”) if the Bond’s stated redemption price at maturity or, in the case of a Discount Bond, the Bond’s “revised issue price”, exceeds the amount for which the U.S. Holder purchased the Bond by at least 0.25 per cent. of the Bond’s stated redemption price at maturity or revised issue price, respectively, multiplied by the number of complete years to the Bond’s maturity (or, in the case of a Bond that is an instalment obligation, the Bond’s weighted average maturity). If this excess is not sufficient to cause the Bond to be a Market Discount Bond, then the excess constitutes “de minimis market discount”. For this purpose, the “revised issue price” of a Bond generally equals its issue price, increased by the amount of any OID that has accrued on the Bond and decreased by the amount of any payments previously made on the Bond that were not qualified stated interest payments.

Under current law, any gain recognised on the maturity or disposition of a Market Discount Bond (including any payment on a Bond that is not qualified stated interest) will be treated as ordinary income to the extent that the gain does not exceed the accrued market discount on the Bond. Alternatively, a U.S. Holder of a Market Discount Bond may elect to include market discount in income currently over the life of the Bond. This election shall apply to all debt instruments with market discount acquired by the electing U.S. Holder on or after the first day of the first taxable year to which the election applies. This election may not be revoked without the consent of the Internal Revenue Service (“**IRS**”). A U.S. Holder of a Market Discount Bond that does not elect to include market discount in income currently will generally be required to defer deductions for interest on borrowings incurred to purchase or carry a Market Discount Bond that is in excess of the interest and OID on the Bond includible in the U.S. Holder’s income, to the extent that this excess interest expense does not exceed the portion of the market discount allocable to the days on which the Market Discount Bond was held by the U.S. Holder.

Under current law, market discount will accrue on a straight-line basis unless the U.S. Holder elects to accrue the market discount on a constant-yield method. This election applies only to the Bond with respect to which it is made and is irrevocable.

### *Election to Treat All Interest as Original Issue Discount*

A U.S. Holder may elect to include in gross income all interest that accrues on a Bond using the constant-yield method described above under “*Original Issue Discount – General*” with certain modifications. For purposes of this election, interest includes stated interest, OID, *de minimis* OID, market discount, *de minimis* market discount and unstated interest, as adjusted by any amortisable bond premium (described below under “*Bonds Purchased at a Premium*”) or acquisition premium. This election will generally apply only to the Bond with respect to which it is made and may not be revoked without the consent of the IRS. If the election to apply the constant-yield method to all interest on a Bond is made with respect to a Market Discount Bond, the electing U.S. Holder will be treated as having made the election discussed above under “*Market Discount*” to include market discount in income currently over the life of all debt instruments with market discount held or thereafter acquired by the U.S. Holder. U.S. Holders should consult their tax advisers concerning the propriety and consequences of this election.

### *Variable Interest Rate Bonds*

Bonds that provide for interest at variable rates (“**Variable Interest Rate Bonds**”) generally will bear interest at a “qualified floating rate” and thus will be treated as “variable rate debt instruments” under Treasury regulations governing accrual of OID. A Variable Interest Rate Bond will qualify as a “variable rate debt instrument” if (a) its issue price does not exceed the total noncontingent principal payments due under the Variable Interest Rate Bond by more than a specified *de minimis* amount and (b) it provides for stated interest, paid or compounded at least annually, at (i) one or more qualified floating rates, (ii) a single fixed rate and one or more qualified floating rates, (iii) a single objective rate, or (iv) a single fixed rate and a single objective rate that is a qualified inverse floating rate.

A “**qualified floating rate**” is any variable rate where variations in the value of the rate can reasonably be expected to measure contemporaneous variations in the cost of newly borrowed funds in the currency in which the Variable Interest Rate Bond is denominated. A fixed multiple of a qualified floating rate will constitute a qualified floating rate only if the multiple is greater than 0.65 but not more than 1.35. A variable rate equal to the product of a qualified floating rate and a fixed multiple that is greater than 0.65 but not more than 1.35, increased or decreased by a fixed rate, will also constitute a qualified floating rate. In addition, two or more qualified floating rates that can reasonably be expected to have approximately the

same values throughout the term of the Variable Interest Rate Bond (e.g. two or more qualified floating rates with values within 25 basis points of each other as determined on the Variable Interest Rate Bond's issue date) will be treated as a single qualified floating rate. Notwithstanding the foregoing, a variable rate that would otherwise constitute a qualified floating rate but which is subject to one or more restrictions such as a maximum numerical limitation (i.e. a cap) or a minimum numerical limitation (i.e. a floor) may, under certain circumstances, fail to be treated as a qualified floating rate unless the cap or floor is fixed throughout the term of the Bond.

An “**objective rate**” is a rate that is not itself a qualified floating rate but which is determined using a single fixed formula and which is based on objective financial or economic information (e.g. one or more qualified floating rates or the yield of actively traded personal property). A rate will not qualify as an objective rate if it is based on information that is within the control of the Issuer (or a related party) or that is unique to the circumstances of the Issuer (or a related party), such as dividends, profits or the value of the Issuer's stock (although a rate does not fail to be an objective rate merely because it is based on the credit quality of the Issuer). Other variable interest rates may be treated as objective rates if so designated by the IRS in the future. Despite the foregoing, a variable rate of interest on a Variable Interest Rate Bond will not constitute an objective rate if it is reasonably expected that the average value of the rate during the first half of the Variable Interest Rate Bond's term will be either significantly less than or significantly greater than the average value of the rate during the final half of the Variable Interest Rate Bond's term. A “**qualified inverse floating rate**” is any objective rate where the rate is equal to a fixed rate minus a qualified floating rate, as long as variations in the rate can reasonably be expected to inversely reflect contemporaneous variations in the qualified floating rate. If a Variable Interest Rate Bond provides for stated interest at a fixed rate for an initial period of one year or less followed by a variable rate that is either a qualified floating rate or an objective rate for a subsequent period and if the variable rate on the Variable Interest Rate Bond's issue date is intended to approximate the fixed rate (e.g., the value of the variable rate on the issue date does not differ from the value of the fixed rate by more than 25 basis points), then the fixed rate and the variable rate together will constitute either a single qualified floating rate or objective rate, as the case may be.

A qualified floating rate or objective rate in effect at any time during the term of the instrument must be set at a “current value” of that rate. A “**current value**” of a rate is the value of the rate on any day that is no earlier than three months prior to the first day on which that value is in effect and no later than one year following that first day.

If a Variable Interest Rate Bond that provides for stated interest at either a single qualified floating rate or a single objective rate throughout the term thereof qualifies as a “variable rate debt instrument”, then any stated interest on the Bond which is unconditionally payable in cash or property (other than debt instruments of the Issuer) at least annually will constitute qualified stated interest and will be taxed accordingly. Thus, a Variable Interest Rate Bond that provides for stated interest at either a single qualified floating rate or a single objective rate throughout the term thereof and that qualifies as a “variable rate debt instrument” will generally not be treated as having been issued with OID unless the Variable Interest Rate Bond is issued at a “true” discount (i.e. at a price below the Bond's stated principal amount) in excess of a specified *de minimis* amount. OID on a Variable Interest Rate Bond arising from “true” discount is allocated to an accrual period using the constant yield method described above by assuming that the variable rate is a fixed rate equal to (i) in the case of a qualified floating rate or qualified inverse floating rate, the value, as of the issue date, of the qualified floating rate or qualified inverse floating rate, or (ii) in the case of an objective rate (other than a qualified inverse floating rate), a fixed rate that reflects the yield that is reasonably expected for the Variable Interest Rate Bond.

In general, any other Variable Interest Rate Bond that qualifies as a “variable rate debt instrument” will be converted into an “equivalent” fixed rate debt instrument for purposes of determining the amount and accrual of OID and qualified stated interest on the Variable Interest Rate Bond. Such a Variable Interest Rate Bond must be converted into an “equivalent” fixed rate debt instrument by substituting any qualified floating rate or qualified inverse floating rate provided for under the terms of the Variable Interest Rate Bond with a fixed rate equal to the value of the qualified floating rate or qualified inverse floating rate, as the case may be, as of the Variable Interest Rate Bond's issue date. Any objective rate (other than a qualified inverse floating rate) provided for under the terms of the Variable Interest Rate Bond is converted into a fixed rate that reflects the yield that is reasonably expected for the Variable Interest Rate Bond. In the case of a Variable Interest Rate Bond that qualifies as a “variable rate debt instrument” and provides for stated interest at a fixed rate in addition to either one or more qualified floating rates or a



qualified inverse floating rate, the fixed rate is initially converted into a qualified floating rate (or a qualified inverse floating rate, if the Variable Interest Rate Bond provides for a qualified inverse floating rate). Under these circumstances, the qualified floating rate or qualified inverse floating rate that replaces the fixed rate must be such that the fair market value of the Variable Interest Rate Bond as of the Variable Interest Rate Bond's issue date is approximately the same as the fair market value of an otherwise identical debt instrument that provides for either the qualified floating rate or qualified inverse floating rate rather than the fixed rate. Subsequent to converting the fixed rate into either a qualified floating rate or a qualified inverse floating rate, the Variable Interest Rate Bond is converted into an "equivalent" fixed rate debt instrument in the manner described above.

Once the Variable Interest Rate Bond is converted into an "equivalent" fixed rate debt instrument pursuant to the foregoing rules, the amount of OID and qualified stated interest, if any, are determined for the "equivalent" fixed rate debt instrument by applying the general OID rules to the "equivalent" fixed rate debt instrument and a U.S. Holder of the Variable Interest Rate Bond will account for the OID and qualified stated interest as if the U.S. Holder held the "equivalent" fixed rate debt instrument. In each accrual period, appropriate adjustments will be made to the amount of qualified stated interest or OID assumed to have been accrued or paid with respect to the "equivalent" fixed rate debt instrument in the event that these amounts differ from the actual amount of interest accrued or paid on the Variable Interest Rate Bond during the accrual period.

If a Variable Interest Rate Bond, such as a Bond the payments on which are determined by reference to an index, does not qualify as a "variable rate debt instrument", then the Variable Interest Rate Bond will be treated as a contingent payment debt obligation. The proper U.S. federal income tax treatment of Variable Interest Rate Bonds that are treated as contingent payment debt obligations will be more fully described in the applicable Final Terms.

#### *Short-Term Bonds*

In general, an individual or other cash basis U.S. Holder of a short-term Bond is not required to accrue OID (as specially defined below for the purposes of this paragraph) for U.S. federal income tax purposes unless it elects to do so (but may be required to include any stated interest in income as the interest is received). Accrual basis U.S. Holders and certain other U.S. Holders are required to accrue OID on Short-Term Bonds on a straight-line basis or, if the U.S. Holder so elects, under the constant-yield method (based on daily compounding). In the case of a U.S. Holder not required and not electing to include OID in income currently, any gain realised on the sale or retirement of the Short-Term Bond will be ordinary income to the extent of the OID accrued on a straight-line basis (unless an election is made to accrue the OID under the constant-yield method) through the date of sale or retirement. U.S. Holders who are not required and do not elect to accrue OID on Short-Term Bonds will be required to defer deductions for interest on borrowings allocable to Short-Term Bonds in an amount not exceeding the deferred income until the deferred income is realised.

For purposes of determining the amount of OID subject to these rules, all interest payments on a Short-Term Bond are included in the Short-Term Bond's stated redemption price at maturity. A U.S. Holder may elect to determine OID on a Short-Term Bond as if the Short-Term Bond had been originally issued to the U.S. Holder at the U.S. Holder's purchase price for the Short-Term Bond. This election shall apply to all obligations with a maturity of one year or less acquired by the U.S. Holder on or after the first day of the first taxable year to which the election applies, and may not be revoked without the consent of the IRS.

#### *Fungible Issue*

The Issuer may, without the consent of the Holders of outstanding Bonds, issue additional Bonds with identical terms. These additional Bonds, even if they are treated for non-tax purposes as part of the same series as the original Bonds, in some cases may be treated as a separate series for U.S. federal income tax purposes. In such case, the new Bonds may be considered to have been issued with OID, even if the original Bonds had no OID, or the additional Bonds may have a greater amount of OID than the original Bonds. These differences may affect the market value of the original Bonds since if the additional Bonds are not otherwise distinguishable from the original Bonds.

#### **Bonds Purchased at a Premium**

A U.S. Holder that purchases a Bond for an amount in excess of its principal amount, or for a Discount Bond, its stated redemption price at maturity, may elect to treat the excess as "amortisable bond

premium”, in which case the amount required to be included in the U.S. Holder’s income each year with respect to interest on the Bond will be reduced by the amount of amortisable bond premium allocable (based on the Bond’s yield to maturity) to that year. Any election to amortise bond premium shall apply to all bonds (other than bonds the interest on which is excludable from gross income for U.S. federal income tax purposes) held by the U.S. Holder at the beginning of the first taxable year to which the election applies or thereafter acquired by the U.S. Holder, and is irrevocable without the consent of the IRS. See also “Original Issue Discount – Election to Treat All Interest as Original Issue Discount”.

### **Purchase, Sale and Retirement of Bonds**

A U.S. Holder’s tax basis in a Bond will generally be its cost, increased by the amount of any OID or market discount included in the U.S. Holder’s income with respect to the Bond and the amount, if any, of income attributable to *de minimis* OID and *de minimis* market discount included in the U.S. Holder’s income with respect to the Bond, and reduced by (i) the amount of any payments that are not qualified stated interest payments, and (ii) the amount of any amortisable bond premium applied to reduce interest on the Bond.

A U.S. Holder will generally recognise gain or loss on the sale or retirement of a Bond equal to the difference between the amount realised on the sale or retirement and the tax basis of the Bond. The amount realised does not include the amount attributable to accrued but unpaid interest, which will be taxable as interest income to the extent not previously included in income. Except to the extent described above under “*Original Issue Discount – Market Discount*” or “*Original Issue Discount – Short-Term Bonds*” or attributable to changes in exchange rates (as discussed below), gain or loss recognised on the sale or retirement of a Bond will be capital gain or loss and will be long-term capital gain or loss if the U.S. Holder’s holding period in the Bonds exceeds one year.

Gain or loss realised by a U.S. Holder on the sale or retirement of a Bond generally will be U.S. source.

### **Foreign Currency Bonds**

#### *Interest*

If an interest payment is denominated in, or determined by reference to, a foreign currency, the amount of income recognised by a cash basis U.S. Holder will be the U.S. dollar value of the interest payment, based on the exchange rate in effect on the date of receipt, regardless of whether the payment is in fact converted into U.S. dollars.

An accrual basis U.S. Holder may determine the amount of income recognised with respect to an interest payment denominated in, or determined by reference to, a foreign currency in accordance with either of two methods. Under the first method, the amount of income accrued will be based on the average exchange rate in effect during the interest accrual period (or, in the case of an accrual period that spans two taxable years of a U.S. Holder, the part of the period within the taxable year).

Under the second method, the U.S. Holder may elect to determine the amount of income accrued on the basis of the exchange rate in effect on the last day of the accrual period (or, in the case of an accrual period that spans two taxable years, the exchange rate in effect on the last day of the part of the period within the taxable year). Additionally, if a payment of interest is actually received within five business days of the last day of the accrual period, an electing accrual basis U.S. Holder may instead translate the accrued interest into U.S. dollars at the exchange rate in effect on the day of actual receipt. Any such election will apply to all debt instruments held by the U.S. Holder at the beginning of the first taxable year to which the election applies or thereafter acquired by the U.S. Holder, and will be irrevocable without the consent of the IRS.

Upon receipt of an interest payment (including a payment attributable to accrued but unpaid interest upon the sale or retirement of a Bond) denominated in, or determined by reference to, a foreign currency, the U.S. Holder may recognise U.S. source exchange gain or loss (taxable as ordinary income or loss) equal to the difference between the amount received (translated into U.S. dollars at the spot rate on the date of receipt) and the amount previously accrued, regardless of whether the payment is in fact converted into U.S. dollars.

### *OID*

OID for each accrual period on a Discount Bond that is denominated in, or determined by reference to, a foreign currency, will be determined in the foreign currency and then translated into U.S. dollars in the same manner as stated interest accrued by an accrual basis U.S. Holder, as described above. Upon receipt of an amount attributable to OID (whether in connection with a payment on the Bond or a sale of the Bond), a U.S. Holder may recognise U.S. source exchange gain or loss (taxable as ordinary income or loss) equal to the difference between the amount received (translated into U.S. dollars at the spot rate on the date of receipt) and the amount previously accrued, regardless of whether the payment is in fact converted into U.S. dollars.

### *Market Discount*

Market Discount on a Bond that is denominated in, or determined by reference to, a foreign currency, will be accrued in the foreign currency. If the U.S. Holder elects to include market discount in income currently, the accrued market discount will be translated into U.S. dollars at the average exchange rate for the accrual period (or portion thereof within the U.S. Holder's taxable year). Upon the receipt of an amount attributable to accrued market discount, the U.S. Holder may recognise U.S. source exchange gain or loss (which will be taxable as ordinary income or loss) determined in the same manner as for accrued interest or OID. A U.S. Holder that does not elect to include market discount in income currently will recognise, upon the disposition or maturity of the Bond, the U.S. dollar value of the amount accrued, calculated at the spot rate on that date, and no part of this accrued market discount will be treated as exchange gain or loss.

### *Bond Premium*

Bond premium (including acquisition premium) on a Bond that is denominated in, or determined by reference to, a foreign currency, will be computed in units of the foreign currency, and any such bond premium that is taken into account currently will reduce interest income in units of the foreign currency. On the date bond premium offsets interest income, a U.S. Holder may recognise U.S. source exchange gain or loss (taxable as ordinary income or loss) measured by the difference between the spot rate in effect on that date, and on the date the Bonds were acquired by the U.S. Holder. A U.S. Holder that does not elect to take bond premium (other than acquisition premium) into account currently will recognise a market loss when the Bond matures.

### *Sale or Retirement*

As discussed above under "*Purchase, Sale and Retirement of Bonds*", a U.S. Holder will generally recognise gain or loss on the sale or retirement of a Bond equal to the difference between the amount realised on the sale or retirement and its tax basis in the Bond. A U.S. Holder's tax basis in a Bond that is denominated in a foreign currency will be determined by reference to the U.S. dollar cost of the Bond. The U.S. dollar cost of a Bond purchased with foreign currency will generally be the U.S. dollar value of the purchase price on the date of purchase or, in the case of Bonds traded on an established securities market, as defined in the applicable Treasury Regulations, that are purchased by a cash basis U.S. Holder (or an accrual basis U.S. Holder that so elects), on the settlement date for the purchase.

The amount realised on a sale or retirement for an amount in foreign currency will be the U.S. dollar value of this amount on the date of sale or retirement or, in the case of Bonds traded on an established securities market, as defined in the applicable Treasury Regulations, sold by a cash basis U.S. Holder (or an accrual basis U.S. Holder that so elects), on the settlement date for the sale. Such an election by an accrual basis U.S. Holder must be applied consistently from year to year and cannot be revoked without the consent of the IRS.

A U.S. Holder will recognise U.S. source exchange rate gain or loss (taxable as ordinary income or loss) on the sale or retirement of a Bond equal to the difference, if any, between the U.S. dollar values of the U.S. Holder's purchase price for the Bond (or, if less, the principal amount of the Bond) (i) on the date of sale or retirement and (ii) the date on which the U.S. Holder acquired the Bond. Any such exchange rate gain or loss will be realised only to the extent of total gain or loss realised on the sale or retirement.

### **Disposition of Foreign Currency**

Foreign currency received as interest on a Bond or on the sale or retirement of a Bond will have a tax basis equal to its U.S. Dollar value at the time the interest is received or at the time of the sale or retirement.

Foreign currency that is purchased will generally have a tax basis equal to the U.S. Dollar value of the foreign currency on the date of purchase. Any gain or loss recognised on a sale or other disposition of a foreign currency (including its use to purchase Bonds or an exchange for U.S. Dollars) will be ordinary income or loss.

### **Backup Withholding and Information Reporting**

In general, payments of interest and accrued OID on, and the proceeds of a sale, redemption or other disposition of, the Bonds, payable to a U.S. Holder by a U.S. paying agent or other U.S. intermediary will be reported to the IRS and to the U.S. Holder as may be required under applicable regulations. Backup withholding will apply to these payments and to accruals of OID if the U.S. Holder fails to provide an accurate taxpayer identification number or certification of exempt status or fails to report all interest and dividends required to be shown on its U.S. federal income tax returns. Certain U.S. Holders (including, among others, corporations) are not subject to backup withholding. U.S. Holders should consult their tax advisers as to their qualification for exemption from backup withholding and the procedure for obtaining an exemption.

### **Reportable Transactions**

U.S. taxpayer that participates in a “**reportable transaction**” will be required to disclose its participation to the IRS. The scope and application of these rules is not entirely clear. A U.S. Holder may be required to treat a foreign currency exchange loss from the Bonds as a reportable transaction if the loss exceeds U.S.\$50,000 in a single taxable year, if the U.S. Holder is an individual or trust, or higher amounts for other non-individual U.S. Holders. In the event the acquisition, holding or disposition of Bonds constitutes participation in a “reportable transaction” for purposes of these rules, a U.S. Holder will be required to disclose its investment by filing Form 8886 with the IRS. Pursuant to U.S. tax legislation enacted in 2004, a penalty in the amount of U.S.\$10,000 in the case of a natural person and U.S.\$50,000 in all other cases is generally imposed on any taxpayer that fails to timely file an information return with the IRS with respect to a transaction resulting in a loss that is treated as a reportable transaction. Accordingly, if a U.S. Holder realises a loss on any Bond (or, possibly, aggregate losses from the Bonds) satisfying the monetary thresholds discussed above, the U.S. Holder could be required to file an information return with the IRS, and failure to do so may subject the U.S. Holder to the penalties described above. In addition, the Issuer and its advisers may also be required to disclose the transaction to the IRS, to maintain a list of U.S. Holders, and to furnish this list and certain other information to the IRS upon written request. Prospective purchasers are urged to consult their tax advisers regarding the application of these rules to the acquisition, holding or disposition of Bonds.

## CHAPTER 15

### SUBSCRIPTION AND SALE AND TRANSFER AND SELLING RESTRICTIONS

The Dealers have, in a programme agreement (the “**Programme Agreement**”) dated 23 July 2002 as amended or supplemented from time to time, agreed with the Obligors a basis upon which they or any of them may from time to time agree to purchase Bonds. Any such agreement will extend to those matters stated under Chapter 8, “*Form of the Bonds*” and Chapter 9, “*Terms and Conditions of the Bonds*”. In the Programme Agreement, each of the Obligors has agreed to reimburse the Dealers for certain of their expenses in connection with the establishment and any future update of the Programme and the issue of Bonds under the Programme and to indemnify the Dealers against certain liabilities incurred by them in connection therewith.

In order to facilitate the offering of any Tranche of the Bonds, certain persons participating in the offering of the Tranche may engage in transactions that stabilise, maintain or otherwise affect the market price of the relevant Bonds during and after the offering of the Tranche. Specifically such persons may over-allot (provided that, in the case of any Tranche of Bonds to be admitted to trading on the Market, the aggregate principal amount of Bonds allotted does not exceed 105 per cent. of the aggregate principal amount of the relevant Tranche) or create a short position in the Bonds for their own account by selling more Bonds than have been sold to them by the Issuer. Such persons may also elect to cover any such short position by purchasing Bonds in the open market. In addition, such persons may stabilise or maintain the price of the Bonds by bidding for or purchasing Bonds in the open market and may impose penalty bids, under which selling concessions allowed to syndicate members or other broker-dealers participating in the offering of the Bonds are reclaimed if Bonds previously distributed in the offering are repurchased in connection with stabilisation transactions or otherwise. The effect of these transactions may be to stabilise or maintain the market price of the Bonds at a level above that which might otherwise prevail in the open market. The imposition of a penalty bid may also affect the price of the Bonds to the extent that it discourages resales thereof. No representation is made as to the magnitude or effect of any such stabilising or other transactions. Such transactions, if commenced, may be discontinued at any time. Under UK laws and regulations permitted stabilising activities may only be carried on by the Stabilising Manager named in the applicable Final Terms or any agent of his and, if begun, may be ended at any time, but it must end no later than the earlier of 30 days after the Issue Date of the relevant Tranche of Bonds and 60 days after the date of the allotment of the relevant Tranche of Bonds.

#### 15.1 Transfer Restrictions

***As a result of the following restrictions, purchasers of Bonds in the United States are advised to consult legal counsel prior to making any purchase, offer, sale, resale or other transfer of such Bonds.***

Each purchaser of Registered Global Bonds (other than a person purchasing an interest in a Registered Global Bond with a view to holding it in the form of an interest in the same Global Bond) or person wishing to transfer an interest from one Registered Global Bond to another will be required to acknowledge, represent and agree as follows (terms used in this paragraph that are defined in Rule 144A or in Regulation S are used herein as defined therein):

- (i) that either (a) it is a QIB, purchasing (or holding) the Bonds for its own account or for the account of one or more QIBs and it is aware, and each beneficial owner of the Bonds has been advised, that any sale to it is being made in reliance on Rule 144A or (b) it is outside the United States, is not a U.S. person and is not an affiliate of the Issuer or a person acting on behalf of such an affiliate;
- (ii) that the Bonds and the guarantees in respect thereof are being offered and sold in a transaction not involving a public offering in the United States within the meaning of the Securities Act, and that the Bonds and the guarantees in respect thereof have not been and will not be registered under the Securities Act or any other applicable U.S. State securities laws and may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons except as set forth below;
- (iii) that, unless it holds an interest in a Regulation S Global Bond and either is a person located outside the United States or is not a U.S. person, if in the future it decides to resell, pledge or otherwise transfer the Bonds or any beneficial interests in the Bonds, it will do so, prior to the date which is two years after the later of the last Issue Date for the Series and the last date on which the Issuer or an affiliate of the Issuer was the owner of such Bonds, only (a) to the Issuer or any affiliate thereof, (b) inside the United States to a person whom the seller reasonably believes is a QIB purchasing

for its own account or for the account of a QIB in a transaction meeting the requirements of Rule 144A, (c) outside the United States in compliance with Rule 903 or Rule 904 under the Securities Act, (d) pursuant to the exemption from registration provided by Rule 144 under the Securities Act (if available) or (e) pursuant to an effective registration statement under the Securities Act, in each case in accordance with all applicable U.S. State securities laws;

- (iv) it will, and will require each subsequent holder to, notify any purchaser of the Bonds from it of the resale restrictions referred to in paragraph (iii) above, if then applicable;
- (v) that Bonds initially offered in the United States to QIBs will be represented by one or more Rule 144A Global Bonds and that Bonds offered outside the United States in reliance on Regulation S will be represented by one or more Regulation S Global Bonds;
- (vi) that the Rule 144A Global Bonds, will bear a legend to the following effect unless otherwise agreed to by the Issuer:

“THIS SECURITY AND THE GUARANTEES IN RESPECT HEREOF HAVE NOT BEEN AND WILL NOT BE REGISTERED UNDER THE U.S. SECURITIES ACT OF 1933, AS AMENDED (THE “SECURITIES ACT”), OR ANY OTHER APPLICABLE U.S. STATE SECURITIES LAWS AND, ACCORDINGLY, MAY NOT BE OFFERED, SOLD, PLEDGED OR OTHERWISE TRANSFERRED WITHIN THE UNITED STATES OR TO, OR FOR THE ACCOUNT OR BENEFIT OF, U.S. PERSONS EXCEPT AS SET FORTH IN THE FOLLOWING SENTENCE. BY ITS ACQUISITION HEREOF, THE HOLDER (A) REPRESENTS THAT IT IS A “QUALIFIED INSTITUTIONAL BUYER” (AS DEFINED IN RULE 144A UNDER THE SECURITIES ACT) PURCHASING THE SECURITIES FOR ITS OWN ACCOUNT OR FOR THE ACCOUNT OF ONE OR MORE QUALIFIED INSTITUTIONAL BUYERS; (B) AGREES THAT IT WILL NOT RESELL OR OTHERWISE TRANSFER THE SECURITIES EXCEPT IN ACCORDANCE WITH THE AGENCY AGREEMENT AND, PRIOR TO THE DATE WHICH IS TWO YEARS AFTER THE LATER OF THE LAST ISSUE DATE FOR THE SERIES AND THE LAST DATE ON WHICH THE ISSUER OR AN AFFILIATE OF THE ISSUER WAS THE OWNER OF SUCH SECURITIES OTHER THAN (1) TO THE ISSUER OR ANY AFFILIATE THEREOF, (2) INSIDE THE UNITED STATES TO A PERSON WHOM THE SELLER REASONABLY BELIEVES IS A QUALIFIED INSTITUTIONAL BUYER WITHIN THE MEANING OF RULE 144A UNDER THE SECURITIES ACT PURCHASING FOR ITS OWN ACCOUNT OR FOR THE ACCOUNT OF A QUALIFIED INSTITUTIONAL BUYER IN A TRANSACTION MEETING THE REQUIREMENTS OF RULE 144A, (3) OUTSIDE THE UNITED STATES IN COMPLIANCE WITH RULE 903 OR RULE 904 UNDER THE SECURITIES ACT, (4) PURSUANT TO THE EXEMPTION FROM REGISTRATION PROVIDED BY RULE 144 UNDER THE SECURITIES ACT (IF AVAILABLE) OR (5) PURSUANT TO AN EFFECTIVE REGISTRATION STATEMENT UNDER THE SECURITIES ACT, IN EACH CASE IN ACCORDANCE WITH ALL APPLICABLE SECURITIES LAWS OF THE STATES OF THE UNITED STATES AND ANY OTHER JURISDICTION; AND (C) IT AGREES THAT IT WILL DELIVER TO EACH PERSON TO WHOM THIS SECURITY IS TRANSFERRED A NOTICE SUBSTANTIALLY TO THE EFFECT OF THIS LEGEND. NO REPRESENTATION CAN BE MADE AS TO THE AVAILABILITY OF THE EXEMPTION PROVIDED BY RULE 144 UNDER THE SECURITIES ACT FOR REALES OF THIS BOND.

THIS SECURITY AND RELATED DOCUMENTATION (INCLUDING, WITHOUT LIMITATION, THE AGENCY AGREEMENT REFERRED TO HEREIN) MAY BE AMENDED OR SUPPLEMENTED FROM TIME TO TIME, WITHOUT THE CONSENT OF, BUT UPON NOTICE TO, THE HOLDERS OF SUCH SECURITIES SENT TO THEIR REGISTERED ADDRESSES, TO MODIFY THE RESTRICTIONS ON AND PROCEDURES FOR REALES AND OTHER TRANSFERS OF THIS SECURITY TO REFLECT ANY CHANGE IN APPLICABLE LAW OR REGULATION (OR THE INTERPRETATION THEREOF) OR IN PRACTICES RELATING TO REALES OR OTHER TRANSFERS OF RESTRICTED SECURITIES GENERALLY. THE HOLDER OF THIS SECURITY SHALL BE DEEMED, BY ITS ACCEPTANCE OR PURCHASE HEREOF, TO HAVE AGREED TO ANY SUCH AMENDMENT OR SUPPLEMENT (EACH OF WHICH SHALL BE CONCLUSIVE AND BINDING ON THE HOLDER HEREOF AND ALL FUTURE HOLDERS OF THIS

SECURITY AND ANY SECURITIES ISSUED IN EXCHANGE OR SUBSTITUTION THEREFOR, WHETHER OR NOT ANY NOTATION THEREOF IS MADE HEREON).”;

- (vii) if it is outside the United States and is not a U.S. person, that if it should resell or otherwise transfer the Bonds prior to the expiration of the distribution compliance period (defined as 40 days after the completion of the distribution of all the Bonds of the tranche of which such Bonds form a part), it will do so only (a)(i) outside the United States in compliance with Rule 903 or 904 under the Securities Act or (ii) to a QIB in compliance with Rule 144A and (b) in accordance with all applicable U.S. State securities laws; and it acknowledges that the Regulation S Global Bonds will bear a legend to the following effect unless otherwise agreed to by the Issuer:

“THIS SECURITY AND THE GUARANTEES IN RESPECT HEREOF HAVE NOT BEEN AND WILL NOT BE REGISTERED UNDER THE U.S. SECURITIES ACT OF 1933, AS AMENDED (THE “SECURITIES ACT”), OR ANY OTHER APPLICABLE U.S. STATE SECURITIES LAWS AND, ACCORDINGLY, MAY NOT BE OFFERED OR SOLD WITHIN THE UNITED STATES OR TO, OR FOR THE ACCOUNT OR BENEFIT OF, U.S. PERSONS EXCEPT IN ACCORDANCE WITH THE AGENCY AGREEMENT AND PURSUANT TO AN EXEMPTION FROM REGISTRATION UNDER THE SECURITIES ACT OR PURSUANT TO AN EFFECTIVE REGISTRATION STATEMENT UNDER THE SECURITIES ACT. THIS LEGEND SHALL CEASE TO APPLY UPON THE EXPIRY OF THE PERIOD OF 40 DAYS AFTER THE COMPLETION OF THE DISTRIBUTION OF ALL THE BONDS OF THE TRANCHE OF WHICH THIS BOND FORMS PART.”; and

- (viii) that the Issuer and others will rely upon the truth and accuracy of the foregoing acknowledgements, representations and agreements and agrees that if any of such acknowledgements, representations or agreements made by it are no longer accurate, it shall promptly notify the Issuer; and if it is acquiring any Bonds as a fiduciary or agent for one or more accounts it represents that it has sole investment discretion with respect to each such account and that it has full power to make the foregoing acknowledgements, representations and agreements on behalf of each such account.

Institutional Accredited Investors who purchase Registered Bonds in definitive form offered and sold in the United States are required to execute and deliver to the Registrar an IAI Investment Letter, except as otherwise specified in the applicable Final Terms. Upon execution and delivery of an IAI Investment Letter by an Institutional Accredited Investor, Bonds will be issued in definitive registered form, see Chapter 8, “*Form of the Bonds*”.

The IAI Investment Letter will state, among other things, the following:

- (i) that the Institutional Accredited Investor has received a copy of the Prospectus and such other information as it deems necessary in order to make its investment decision;
- (ii) that the Institutional Accredited Investor is an Institutional Accredited Investor within the meaning of Rule 501(a)(1), (2), (3) or (7) of Regulation D under the Securities Act and has such knowledge and experience in financial and business matters as to be capable of evaluating the merits and risks of its investment in the Bonds, and it and any accounts for which it is acting are each able to bear the economic risk of its or any such accounts’ investment for an indefinite period of time;
- (iii) that, in the normal course of its business, the Institutional Accredited Investor invests in or purchases securities similar to the Bonds and that the Institutional Accredited Investor is acquiring the Bonds purchased by it for its own account or for one or more accounts (each of which is an Institutional Accredited Investor) as to each of which it exercises sole investment discretion over and not with a view to any distribution of the Bonds, subject, nevertheless, to the understanding that the disposition of its property shall at all times be and remain within its control;
- (iv) that the Bonds and the guarantees in respect thereof are being offered and sold in a transaction not involving a public offering in the United States within the meaning of the Securities Act, and that the Bonds and the guarantees in respect thereof have not been and will not be registered under the Securities Act or any other applicable U.S. State securities laws and may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons except as set forth below;

- (v) that if in the future it decides to resell, pledge or otherwise transfer the Bonds or any beneficial interests in the Bonds, it will do so, prior to the date which is two years after the later of the last Issue Date for the Series and the last date on which the Issuer or an affiliate of the Issuer was the owner of such Bonds, only (a) to the Issuer or any affiliate thereof, (b) inside the United States to a person whom the seller reasonably believes is a QIB purchasing for its own account or for the account of a QIB in a transaction meeting the requirements of Rule 144A, (c) outside the United States in compliance with Rule 903 or Rule 904 under the Securities Act, (d) to another Institutional Accredited Investor, subject to delivery to the Registrar of a Transfer Certificate to the effect that such transfer is being made to an Institutional Accredited Investor, together with a duly executed IAI Investment Letter from the relevant transferee, (e) pursuant to the exemption from registration provided by Rule 144 under the Securities Act (if available) or (f) pursuant to an effective registration statement under the Securities Act, in each case in accordance with all applicable U.S. State securities laws;
- (vi) it will, and will require each subsequent holder to, notify any purchaser of the Bonds from it of the resale restrictions referred to in paragraph (v) above, if then applicable;
- (vii) that Bonds offered to Institutional Accredited Investors will be in the form of Definitive IAI Registered Bonds;
- (viii) that the Bonds will bear a legend to the following effect unless otherwise agreed to by the Issuer:

“THIS SECURITY AND THE GUARANTEES IN RESPECT HEREOF HAVE NOT BEEN AND WILL NOT BE REGISTERED UNDER THE U.S. SECURITIES ACT OF 1933, AS AMENDED (THE “SECURITIES ACT”), OR ANY OTHER APPLICABLE U.S. STATE SECURITIES LAWS AND, ACCORDINGLY, MAY NOT BE OFFERED, SOLD, PLEDGED OR OTHERWISE TRANSFERRED WITHIN THE UNITED STATES OR TO, OR FOR THE ACCOUNT OR BENEFIT OF, U.S. PERSONS EXCEPT AS SET FORTH IN THE FOLLOWING SENTENCE. BY ITS ACQUISITION HEREOF, THE HOLDER (A) REPRESENTS THAT IT IS AN INSTITUTIONAL “ACCREDITED INVESTOR” (AS DEFINED IN RULE 501(A)(1), (2), (3) OR (7) UNDER THE SECURITIES ACT) (AN “INSTITUTIONAL ACCREDITED INVESTOR”); (B) AGREES THAT IT WILL NOT RESELL OR OTHERWISE TRANSFER THE SECURITIES EXCEPT IN ACCORDANCE WITH THE AGENCY AGREEMENT AND, PRIOR TO THE DATE WHICH IS TWO YEARS AFTER THE LATER OF THE LAST ISSUE DATE FOR THE SERIES AND THE LAST DATE ON WHICH THE ISSUER OR AN AFFILIATE OF THE ISSUER WAS THE OWNER OF SUCH SECURITIES OTHER THAN (1) TO THE ISSUER OR ANY AFFILIATE THEREOF, (2) INSIDE THE UNITED STATES TO A PERSON WHOM THE SELLER REASONABLY BELIEVES IS A QUALIFIED INSTITUTIONAL BUYER WITHIN THE MEANING OF RULE 144A UNDER THE SECURITIES ACT PURCHASING FOR ITS OWN ACCOUNT OR FOR THE ACCOUNT OF A QUALIFIED INSTITUTIONAL BUYER IN A TRANSACTION MEETING THE REQUIREMENTS OF RULE 144A, (3) OUTSIDE THE UNITED STATES IN COMPLIANCE WITH RULE 903 OR RULE 904 UNDER THE SECURITIES ACT, (4) TO ANOTHER INSTITUTIONAL ACCREDITED INVESTOR, SUBJECT TO DELIVERY TO THE REGISTRAR OF A TRANSFER CERTIFICATE TO THE EFFECT THAT SUCH TRANSFER IS BEING MADE TO AN INSTITUTIONAL ACCREDITED INVESTOR, TOGETHER WITH A DULY EXECUTED IAI INVESTMENT LETTER FROM THE RELEVANT TRANSFEREE; (5) PURSUANT TO THE EXEMPTION FROM REGISTRATION PROVIDED BY RULE 144 UNDER THE SECURITIES ACT (IF AVAILABLE) OR (6) PURSUANT TO AN EFFECTIVE REGISTRATION STATEMENT UNDER THE SECURITIES ACT, IN EACH CASE IN ACCORDANCE WITH ALL APPLICABLE SECURITIES LAWS OF THE STATES OF THE UNITED STATES AND ANY OTHER JURISDICTION; AND (C) IT AGREES THAT IT WILL DELIVER TO EACH PERSON TO WHOM THIS SECURITY IS TRANSFERRED A NOTICE SUBSTANTIALLY TO THE EFFECT OF THIS LEGEND. NO REPRESENTATION CAN BE MADE AS TO THE AVAILABILITY OF THE EXEMPTION PROVIDED BY RULE 144 UNDER THE SECURITIES ACT FOR REALES OF THIS DEFINITIVE BOND.

THIS SECURITY AND RELATED DOCUMENTATION (INCLUDING, WITHOUT LIMITATION, THE AGENCY AGREEMENT REFERRED TO HEREIN) MAY BE



AMENDED OR SUPPLEMENTED FROM TIME TO TIME, WITHOUT THE CONSENT OF, BUT UPON NOTICE TO, THE HOLDERS OF SUCH SECURITIES SENT TO THEIR REGISTERED ADDRESSES, TO MODIFY THE RESTRICTIONS ON AND PROCEDURES FOR REALES AND OTHER TRANSFERS OF THIS SECURITY TO REFLECT ANY CHANGE IN APPLICABLE LAW OR REGULATION (OR THE INTERPRETATION THEREOF) OR IN PRACTICES RELATING TO REALES OR OTHER TRANSFERS OF RESTRICTED SECURITIES GENERALLY. THE HOLDER OF THIS SECURITY SHALL BE DEEMED, BY ITS ACCEPTANCE OR PURCHASE HEREOF, TO HAVE AGREED TO ANY SUCH AMENDMENT OR SUPPLEMENT (EACH OF WHICH SHALL BE CONCLUSIVE AND BINDING ON THE HOLDER HEREOF AND ALL FUTURE HOLDERS OF THIS SECURITY AND ANY SECURITIES ISSUED IN EXCHANGE OR SUBSTITUTION THEREFOR, WHETHER OR NOT ANY NOTATION THEREOF IS MADE HEREON).”; and

- (ix) that, in the event that the Institutional Accredited Investor purchases Bonds, it will acquire Bonds having a minimum purchase price of at least U.S.\$500,000 (or the approximate equivalent in another Specified Currency).

No sale of Legended Bonds in the United States to any one purchaser will be for less than U.S.\$100,000 (or its foreign currency equivalent) principal amount or, in the case of sales to Institutional Accredited Investors, U.S.\$500,000 (or its foreign currency equivalent) principal amount and no Legended Bond will be issued in connection with such a sale in a smaller principal amount. If the purchaser is a non-bank fiduciary acting on behalf of others, each person for whom it is acting must purchase at least U.S.\$100,000 (or its foreign currency equivalent) or, in the case of sales to Institutional Accredited Investors, U.S.\$500,000 (or its foreign currency equivalent) principal amount of Registered Bonds.

## 15.2 Selling Restrictions

### 15.2.1 United States

The Bonds and the guarantees in respect thereof have not been and will not be registered under the Securities Act and may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons except in certain transactions exempt from the registration requirements of the Securities Act. Terms in this paragraph have the meanings given to them by Regulation S.

The Bonds in bearer form are subject to U.S. tax law requirements and may not be offered, sold or delivered within the United States or its possessions or to a United States person, except in certain transactions permitted by U.S. tax regulations. Terms used in this paragraph have the meanings given to them by the U.S. Internal Revenue Code of 1986 and regulations thereunder.

In connection with any Bonds which are offered or sold outside the United States in reliance on an exemption from the registration requirements of the Securities Act provided under Regulation S (“**Regulation S Bonds**”), each Dealer has represented and agreed, and each further Dealer appointed under the Programme will be required to represent and agree, that it will not offer or sell or in the case of bearer bonds, deliver such Regulation S Bonds (i) as part of their distribution at any time or (ii) otherwise until 40 days after the completion of the distribution, as determined and certified by the relevant Dealer or, in the case of an issue of Bonds on a syndicated basis, the relevant lead manager, of all Bonds of the Tranche of which such Regulation S Bonds are a part, within the United States or to, or for the account or benefit of, U.S. persons. Each Dealer has further agreed, and each further Dealer appointed under the Programme will be required to agree, that it will send to each dealer to which it sells any Regulation S Bonds during the distribution compliance period a confirmation or other notice setting forth the restrictions on offers and sales of the Regulation S Bonds within the United States or to, or for the account or benefit of, U.S. persons. Terms in this paragraph have the meanings given to them by Regulation S.

Until 40 days after the commencement of the offering of any Series of Bonds, an offer or sale of such Bonds within the United States by any dealer that is not participating in the offering may violate the registration requirements of the Securities Act if such offer or sale is made otherwise than in accordance with an available exemption from registration under the Securities Act.

Dealers may directly or through their respective U.S. broker-dealer affiliates arrange for the offer and resale of Bonds to QIBs pursuant to Rule 144A and each such purchaser of Bonds is hereby notified that the Dealers may be relying on the exemption from the registration requirements of the

Securities Act provided by Rule 144A. The minimum aggregate principal amount of Bonds which may be purchased by a QIB pursuant to Rule 144A is U.S.\$100,000 (or the approximate equivalent thereof in any other currency). To the extent that the Issuer is not subject to or does not comply with the reporting requirements of Section 13 or 15(d) of the Exchange Act or the information furnishing requirements of Rule 12g3-2(b) thereunder, the Issuer and each of the Obligors have agreed to furnish to holders of Bonds and to prospective purchasers designated by such holders, upon request, such information as may be required by Rule 144A(d)(4).

Each issuance of Index Linked Bonds or Dual Currency Bonds shall be subject to such additional U.S. selling restrictions as the Issuer and the relevant Dealer may agree as a term of the issuance and purchase of such Bonds, which additional selling restrictions shall be set out in the applicable Final Terms.

### 15.2.2 European Economic Area

In relation to each Member State of the European Economic Area which has implemented the Prospectus Directive (each, a “**Relevant Member State**”), each Dealer has represented and agreed, and each further Dealer appointed under the Programme will be required to represent and agree, that with effect from and including the date on which the Prospectus Directive is implemented in that Relevant Member State (the “**Relevant Implementation Date**”) it has not made and will not make an offer of Bonds to the public in that Relevant Member State except that it may, with effect from and including the Relevant Implementation Date, make an offer of Bonds to the public in that Relevant Member State:

- (a) in (or in Germany, where the offer starts within) the period beginning on the date of publication of a prospectus in relation to those Bonds which has been approved by the competent authority in that Relevant Member State or, where appropriate, approved in another Relevant Member State and notified to the competent authority in that Relevant Member State, all in accordance with the Prospectus Directive and ending on the date which is 12 months after the date of such publication;
- (b) at any time to legal entities which are authorised or regulated to operate in the financial markets or, if not so authorised or regulated, whose corporate purpose is solely to invest in securities;
- (c) at any time to any legal entity which has two or more of (1) an average of at least 250 employees during the last financial year; (2) a total balance sheet of more than €43,000,000 and (3) an annual net turnover of more than €50,000,000, as shown in its last annual or consolidated accounts; or
- (d) at any time in any other circumstances which do not require the publication by the Issuer of a prospectus pursuant to Article 3 of the Prospectus Directive.

For the purposes of this provision, the expression an “offer of Bonds to the public” in relation to any Bonds in any Relevant Member State means the communication in any form and by any means of sufficient information on the terms of the offer and the Bonds to be offered so as to enable an investor to decide to purchase or subscribe the Bonds, as the same may be varied in that Member State by any measure implementing the Prospectus Directive in that Member State and the expression “Prospectus Directive” means Directive 2003/71/EC and includes any relevant implementing measure in each Relevant Member State.

### 15.2.3 United Kingdom

Each Dealer has represented and agreed and each further Dealer appointed under the Programme will be required to represent and agree that:

- (i) in relation to any Bonds having a maturity of less than one year from the date of issue, (a) it is a person whose ordinary activities involve it in acquiring, holding, managing or disposing of investments (as principal or agent) for the purposes of its business and (b) it has not offered or sold and will not offer or sell any Bonds other than to persons whose ordinary activities involve them in acquiring, holding, managing or disposing of investments (as principal or agent) for the purposes of their businesses or who it is

reasonable to expect will acquire, hold, manage or dispose of investments (as principal or agent) for the purposes of their businesses where the issue of the Bonds would otherwise constitute a contravention of Section 19 of the FSMA by the Issuer;

- (ii) it has only communicated or caused to be communicated and will only communicate or cause to be communicated an invitation or inducement to engage in investment activity (within the meaning of Section 21 of the FSMA) in connection with the issue or sale of any Bonds in circumstances in which Section 21(1) of the FSMA does not or would not otherwise apply to the Obligors; and
- (iii) it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to any Bonds in, from or otherwise involving the United Kingdom.

#### **15.2.4 Cayman Islands**

No invitation or solicitation will be made to the public in the Cayman Islands to subscribe for the Bonds.

#### **15.2.5 Japan**

The Bonds have not been and will not be registered under the Securities and Exchange Law of Japan (the “**Securities and Exchange Law**”). Accordingly, each Dealer has represented, warranted and agreed that it has not, directly or indirectly, offered or sold and will not, directly or indirectly, offer or sell any Bonds in Japan or to, or for the benefit of, any resident of Japan (which term as used herein means any person resident in Japan, including any corporation or other entity organised under the laws of Japan), or to others for re-offering or resale, directly or indirectly, in Japan or to or for the benefit of, any resident of Japan except pursuant to an exemption from the registration requirements of, and otherwise in compliance with, the Securities and Exchange Law and other relevant laws and regulations of Japan.

#### **15.2.6 The Netherlands**

Zero coupon Bonds in definitive form and other Bonds in definitive form on which interest does not become due and payable during their term but only at maturity (savings certificates or *spaarbewijzen* as defined in the Dutch Savings Certificates Act or *Wet inzake spaarbewijzen*, (the “**SCA**”)) may only be transferred and accepted, directly or indirectly, within, from or into the Netherlands through the mediation of either the Issuer or a member of Euronext Amsterdam N.V. with due observance of the provisions of the SCA and its implementing regulations (which include registration requirements). No such mediation is required, however, in respect of (i) the initial issue of such Bonds to the first holders thereof, (ii) the transfer and acceptance by individuals who do not act in the conduct of a profession or business, and (iii) the issue and trading of such Bonds if they are physically issued outside the Netherlands and are not immediately thereafter distributed in The Netherlands.

Each Dealer has furthermore represented and agreed and each further Dealer appointed under the Programme will be required to represent and agree that Bonds with a maturity of less than 12 months which qualify as money market instruments will only be offered, directly or indirectly, in or from the Netherlands, (i) if they each have a minimum denomination (or minimum aggregate purchase price) of €50,000 or the equivalent thereof in another currency; or (ii) solely to persons who trade or invest in securities in the conduct of their profession or business (which includes banks, securities firms, investment institutions, insurance companies, pension funds, other institutional investors, and finance companies and large enterprises which as an ancillary activity regularly invest in securities); or (iii) in circumstances where another exception to or exemption or dispensation from the prohibition of section 3, subsection 4 of the Dutch Act on the Supervision of the Securities Trade 1995 (*Wet toezicht effectenverkeer 1995*) applies.

#### **15.2.7 General**

Each Dealer has agreed and each further Dealer appointed under the Programme will be required to agree that it will (to the best of its knowledge and belief) comply with all applicable securities laws and regulations in force in any jurisdiction in which it purchases, offers, sells or delivers Bonds or possesses or distributes this Prospectus and will obtain any consent, approval or

permission required by it for the purchase, offer, sale or delivery by it of Bonds under the laws and regulations in force in any jurisdiction to which it is subject or in which it makes such purchases, offers, sales or deliveries and none of the Obligors, the Bond Trustee nor any of the other Dealers shall have any responsibility therefor.

None of the Obligors, the Bond Trustee nor the Dealers represents that Bonds may at any time lawfully be sold in compliance with any applicable registration or other requirements in any jurisdiction, or pursuant to any exemption available thereunder, or assumes any responsibility for facilitating such sale.

With regard to each Tranche, the relevant Dealer will be required to comply with such other restrictions as the Issuer and the relevant Dealer shall agree and as shall be set out in the applicable Final Terms.

## CHAPTER 16

### GENERAL INFORMATION

#### 16.1 Authorisation

The establishment of the Programme and the issue of Bonds thereunder have been duly authorised by resolutions of the Board of Directors of the Issuer dated 25 June 2002, 10 June 2003, 27 July 2004, 21 February 2005, 2 March 2005, 13 April 2005 and 22 September 2005. The Issuer has obtained or will obtain from time to time all necessary consents, approvals and authorisations in connection with the issue and performance of the Bonds.

The giving of the Guarantee by each of Anglian Water, Anglian Water Services Holdings Ltd and Anglian Water Services Overseas Holdings Ltd has been duly authorised by resolutions of the Board of Directors of each of Anglian Water, Anglian Water Services Holdings Ltd and Anglian Water Services Overseas Holdings Ltd, respectively, dated 25 June 2002 and 10 June 2003.

The issue of the Initial Bond Policy by MBIA in respect of the first Series of Class A Wrapped Bonds issued under the Programme on the Effective Date was duly authorised by a resolution of the meeting of the board of directors of MBIA passed on 1 March 2002.

#### 16.2 Listing of Bonds

The admission of the Bonds to the Official List will be expressed as a percentage of their nominal amount (excluding accrued interest). It is expected that each Tranche of Bonds which is to be admitted to the Official List and to trading on the Market will be admitted separately as and when issued, subject only to the issue of a Global Bond or Bonds initially representing the Bonds of such Tranche. The listing of the Programme in respect of Bonds was granted on 23 July 2002 and updated on 24 June 2003, 28 July 2004 and 23 September 2005.

#### 16.3 Documents Available

So long as Bonds are capable of being issued under the Programme, copies of the following documents will, when published, be available from the Anglian Water headquarters at Anglian House, Ambury Road, Huntingdon, Cambridgeshire PE29 3NZ, and from the specified offices of the Paying Agents for the time being:

- (i) the Memorandum and Articles of Association of each of the Issuer and the other Obligors;
- (ii) the audited consolidated and non-consolidated (as the case may be) financial statements of Anglian Water for each of the three years ended 31 March 2005, the audited financial statements in respect of the Issuer and Anglian Water Services Holdings Ltd for each of the three financial years ended 31 March 2005 and the audited financial statements in respect of Anglian Water Services Overseas Holdings Ltd for the two financial years ended 31 March 2005 and the period ended 31 March 2003;
- (iii) the most recently published unaudited interim financial statements (if any) of each Obligor;
- (iv) the Programme Agreement, the Agency Agreement, the Bond Trust Deed, the Security Trust Deed and the forms of the Global Bonds, the Bonds in definitive form, the Receipts, the Coupons and the Talons;
- (v) a copy of the Offering Circular dated 23 July 2002;
- (vi) a copy of the Offering Circular dated 24 June 2003;
- (vii) a copy of the Offering Circular dated 28 July 2004;
- (viii) a copy of this Prospectus;
- (ix) in the case of Bonds in issue, the relevant Final Terms;

- (x) any future offering circulars, prospectuses, information memoranda and supplements including Final Terms (save that a set of Final Terms relating to an unlisted Bond will only be available for inspection by a holder of such Bond and such holder must produce evidence satisfactory to the Issuer and the Paying Agent as to its holding of Bonds and identity) to this Prospectus and any other documents incorporated herein or therein by reference;
- (xi) each Bond Policy and all related Endorsements relating to each Tranche of Wrapped Bonds issued under the Programme;
- (xii) in the case of each issue of listed Bonds subscribed pursuant to a subscription agreement, the subscription agreement (or equivalent document);
- (xiii) the Common Terms Agreement;
- (xiv) the Security Agreement;
- (xv) the STID;
- (xvi) each Liquidity Facility Agreement;
- (xvii) each Hedging Agreement;
- (xviii) the Authorised Loan Agreement;
- (xix) the Existing Finance Leases;
- (xx) the I&I Agreements; and
- (xxi) the Master Definitions Agreement.

#### **16.4 Clearing Systems**

The Bonds in bearer form have been accepted for clearance through Euroclear and Clearstream, Luxembourg. The appropriate Common Code and ISIN for each Tranche of Bearer Bonds allocated by Euroclear and Clearstream, Luxembourg will be specified in the applicable Final Terms. In addition, the Issuer may make an application for any Bonds in registered form to be accepted for trading in book-entry form by DTC. The CUSIP and/or CINS numbers for each Tranche of Registered Bonds, together with the relevant ISIN and common code, will be specified in the applicable Final Terms. If the Bonds are to clear through an additional or alternative clearing system (including Sicovam) the appropriate information will be specified in the applicable Final Terms.

The address of Euroclear is 1 Boulevard du Roi Albert II, B-1210 Brussels, Belgium and the address of Clearstream, Luxembourg is 42 Avenue JF Kennedy L-1855 Luxembourg. The address of any alternative clearing system will be specified in the applicable Final Terms.

#### **16.5 Significant or Material Change**

There has been no significant change in the consolidated financial or trading position of Anglian Water and its subsidiary undertakings, nor any material adverse change in the financial position or prospects of Anglian Water, since 31 March 2005.

There has been no material adverse change in the financial position or prospects of each of the Issuer, Anglian Water Services Holdings Ltd or Anglian Water Services Overseas Holdings Ltd since 31 March 2005.

#### **16.6 Litigation**

None of the Obligors is or has been involved in any governmental, legal or arbitration proceedings (including any such proceedings which are pending or threatened of which any of the Obligors is aware) during the 12 months preceding the date of this Prospectus which may have or have had in the recent past significant effects on the financial position or profitability of any of the Obligors or any of their respective groups.

## 16.7 Auditors

PricewaterhouseCoopers LLP, Chartered Accountants and Registered Auditors, (a member of the Institute of Chartered Accountants in England and Wales), of Cornwall Court, 19 Cornwall Street, Birmingham B3 2DT, have audited, without qualification, the consolidated financial statements of Anglian Water for the years ended 31 March 2005, 31 March 2004 (including consolidated comparatives for the year ended 31 March 2003) and the financial statements of the Issuer and Anglian Water Services Holdings Ltd for each of the three years ended 31 March 2005 in accordance with generally accepted auditing standards in the United Kingdom. PricewaterhouseCoopers LLP, Chartered Accountants and Registered Auditors, have audited, without qualification, the non-consolidated financial statements of Anglian Water for the year ended 31 March 2003 in accordance with generally accepted auditing standards in the United Kingdom.

Anglian Water Services Overseas Holdings Ltd, being an exempted company incorporated with limited liability under the laws of the Cayman Islands, is not obliged by statute to prepare audited accounts. Anglian Water Services Overseas Holdings Ltd has nevertheless prepared its financial statements for each of the two years year ended 31 March 2005 and the period ended 31 March 2003. These financial statements have been audited, without qualification, by PricewaterhouseCoopers LLP, Chartered Accountants and Registered Auditors (a member of the Institute of Chartered Accountants in England and Wales), in accordance with generally accepted auditing standards in the United Kingdom.

The reports of PricewaterhouseCoopers LLP each dated 1 June 2005 (in respect of year ended 31 March 2005) and 2 June 2004 (in respect of year ended 31 March 2004) in respect, in each case of (i) Anglian Water, (ii) the Issuer and (iii) Anglian Water Services Holdings Ltd stated that the reports, including the opinions, have been prepared for, and only for, the respective company's member in accordance with Section 235 of the Companies Act 1985 and for no other purpose, and that PricewaterhouseCoopers LLP did not, in giving their opinions, accept or assume responsibility for any other purpose or to any other person to whom the reports are shown or into whose hands the reports may come save where expressly agreed by PricewaterhouseCoopers LLP's prior consent in writing.

The reports of PricewaterhouseCoopers LLP each dated 1 June 2005 and 2 June 2004 in respect of Anglian Water Services Overseas Holdings Ltd for the periods ended 31 March 2005 and 31 March 2004 respectively stated that the reports, including the opinions, have been prepared for and only for the company's member for the purpose of management and for no other purpose, and that PricewaterhouseCoopers LLP did not, in giving their opinions, accept or assume responsibility for any other purpose or to any other person to whom the report is shown or into whose hands the report may come save where expressly agreed by PricewaterhouseCoopers LLP's prior consent in writing.

## 16.8 Bond Trustee's reliance on reports and legal opinions

Certain of the reports of accountants and other experts to be provided in connection with the Programme and/or the issue of Bonds thereunder may be provided on terms whereby they contain a limit on the liability of such accountants or other experts.

Under the terms of the Programme, the Bond Trustee will not necessarily receive a legal opinion in connection with each issue of Bonds.

As at the Effective Date, the Bond Trustee had been provided with a legal opinion outlining the anticipated tax treatment of AWG Group Ltd, the Issuer and other members of the AWG Group in relation to, *inter alia*, the extinguishment of existing AWG Group borrowings or their assumption by the Issuer, the Anglian Water Loan Notes and the Hedging Agreements. This legal opinion included certain conclusions on the tax treatment of AWG Group Ltd, Anglian Water and the Issuer in relation to these transactions, and these conclusions would have been made in reliance on the conformity with U.K. GAAP of accounting treatment outlined in an AWG accounting report. This accounting report was prepared by the accounting department of AWG and was not reviewed or approved by PricewaterhouseCoopers LLP, auditors of AWG Group Ltd and the members of the AWG Group at the date of such legal opinion.

#### **16.9 Information in respect of the Bonds**

The issue price and the amount of the relevant Bonds will be determined, before filing of the relevant Final Terms of each Tranche, based on then prevailing market conditions. The Issuer does not intend to provide any post-issuance information in relation to any issues of Bonds, but see the Common Terms Agreement for details of the Investors Report.

#### **16.10 Material Contracts**

Anglian Water has not entered into contracts outside the ordinary course of the its business, which could result in Anglian Water or any member of its group being under an obligation or entitlement that is material to Anglian Water's ability to meet its obligation to holders of Bonds in respect of the Bonds being issued.

#### **16.11 Third Party Information**

Information contained in this Prospectus which is sourced from Ofwat has been accurately reproduced and, as far as the Issuer is aware and is able to ascertain from information published by Ofwat, no facts have been omitted which would render the reproduced information inaccurate or misleading. The Issuer has also identified the source(s) of such information.



## CHAPTER 17

### SUMMARY OF CERTAIN SIGNIFICANT DIFFERENCES BETWEEN U.K. GAAP AND U.S. GAAP

The financial statements of Anglian Water have been prepared in accordance with U.K. GAAP, which differs in certain respects from U.S. GAAP. A description of certain material differences between relevant accounting principles is provided below.

Management has not quantified the effect of the differences between U.K. GAAP and U.S. GAAP on the profits or shareholders' funds of Anglian Water. Had we undertaken such quantification or reconciliation, other potential accounting and disclosure differences may have come to our attention, which are not identified below. Accordingly there can be no assurances that such profits or shareholders' funds determined in accordance with U.K. GAAP would not be different if they had been determined under U.S. GAAP.

This summary should not be taken as a complete list of all differences between U.K. GAAP and U.S. GAAP. No attempt has been made to identify all disclosures, presentations or classifications that would affect the manner in which transactions or events are presented in the financial statements or notes thereto.

Further, no attempt has been made to identify future differences between U.K. GAAP and U.S. GAAP as the result of prescribed changes in accounting standards. Regulatory bodies that promulgate U.K. GAAP and U.S. GAAP have significant projects ongoing that could affect future comparisons such as this one between U.K. GAAP and U.S. GAAP. Future developments or changes in either U.K. GAAP or U.S. GAAP may give rise to additional differences between U.K. GAAP and U.S. GAAP, which could have a significant impact on Anglian Water.

In making an investment decision, investors must rely upon their own examination of the Obligors, the terms of the Bonds being offered and the financial information set forth in this Prospectus. Potential investors should consult their own professional advisers for an understanding of the differences that might affect the financial information herein.

#### **Water and sewerage infrastructure assets**

In accordance with accepted practice in the U.K. water industry, investment expenditure on infrastructure assets (as defined in Anglian Water's accounting policies) relating to increases in capacity or enhancements of the network and on maintaining the operating capability of the network in accordance with defined standards of service, is treated as an addition to tangible fixed assets at cost. The depreciation charge for infrastructure assets is the estimated level of annual expenditure required to maintain the operating capability of the network which is based on Anglian Water's independently certified asset management plan.

Under U.S. GAAP, any expenditure on the maintenance of infrastructure assets would be expensed as incurred. Depreciation would be calculated for infrastructure assets and would be depreciated over their expected useful lives, as opposed to estimating depreciation based on the infrastructure renewals charge.

#### **Grants and contributions**

In accordance with accepted practice in the U.K. water industry, grants and capital contributions received in respect of infrastructure assets are deducted from the cost of these assets. This policy is not in accordance with the provisions of the Companies Act 1985 but has been adopted to show a true and fair view as while a provision is made for depreciation of infrastructure assets on the basis stated above, these assets have no determinable finite economic life and hence no basis exists on which to recognise such contributions as deferred income. Grants and capital contributions in respect of other capital expenditure are credited to a deferred income account and released to the profit and loss account over the expected useful economic life of the relevant asset.

Under U.S. GAAP, such grants and contributions may either be deducted from the cost of the asset or deferred as a credit and amortised over the useful life of the asset.

#### **Recoverability of fixed assets**

Under U.K. GAAP, periodic recoverability tests are performed on tangible fixed assets. FRS 11 "Impairment of Fixed Assets and Goodwill" sets out detailed methods for measuring and recognising impairment losses. The impairment review compares the carrying value of fixed assets or goodwill with their recoverable amount, being the higher of net realisable value and value in use (based on present value calculations). For goodwill, the

impairment review is required in the financial year following the financial year in which the acquisition was made. Thereafter impairment tests are only performed where there is an indication (or triggering event) that the fixed asset or goodwill may be subject to impairment.

Under U.S. GAAP, SFAS 144 “Accounting for the Impairment or Disposal of Long-Lived Assets” (“SFAS 144”) develops a single accounting method under which long-lived assets that are to be disposed by sale are measured at the lower of book value or fair value less costs to sell. SFAS 144 requires that impairments of long-lived assets are recognised when the carrying value of an asset or group of assets exceeds the undiscounted cash flows expected to result from the use of the assets, and is measured by comparing the carrying value of an asset or group of assets against their discounted cash flows. SFAS 144 does not apply to goodwill and certain other intangible assets.

#### **Transfers of assets between parties under common control**

Under U.K. GAAP, transfers of assets between parties under common control depend on the type of transaction that has occurred. In general terms, U.K. GAAP accounts for such transactions at fair value.

Under U.S. GAAP, the treatment of the transfer of assets between parties under common control depends on the nature of the transaction. If the transfer is a recurring transaction, such as routine inventory transfers, the exchange price is normally used regardless of whether a common control relationship exists. If the transfer is a non-recurring transaction, such as transfers of long-lived assets including real estate, generally the assets received are normally recorded at historical cost predecessor basis.

#### **Capitalisation of borrowing costs**

Anglian Water expenses all borrowing costs and, accordingly, does not capitalise any borrowing costs associated with the funding of the construction of fixed assets.

Under U.S. GAAP, the borrowing costs of funds used to finance the construction of major qualifying assets must be capitalised up to the date the assets are ready for use, and then amortised over the average life of the assets. The amount to be capitalised is an allocation of the interest cost incurred during the period required to complete the asset. The interest rate for capitalisation purposes is based on the interest rates of the entity’s outstanding borrowings. If a specific new borrowing is associated with the asset the rate on that borrowing may be applied to the appropriate portion of the expenditure for that asset.

#### **Leases**

While U.S. GAAP is similar in concept to U.K. GAAP its detailed requirements are more extensive and differences exist. Leases classified as finance leases under U.K. GAAP are likely to be classified as capital leases under U.S. GAAP. Certain operating leases under U.K. GAAP, however, may also be classified as capital leases under U.S. GAAP depending on the specific terms and conditions attaching to the lease.

#### **Pensions**

Under U.K. GAAP, defined benefit schemes are accounted for in accordance with SSAP 24 “Accounting for Pension Costs” (“SSAP 24”). SSAP 24 aims to produce, for purposes of defined benefit schemes, an estimate of cost, based on long-term actuarial assumptions under a triennial actuarial valuation. The schemes’ assets are valued based on the discounted value of expected future dividend/investment income using a long-term risk adjusted discount rate, rather than on a market value basis. Asset valuation methods are consistent with the method and assumptions used to value the liabilities to pay future pensions (i.e. the discount and long-term return on assets are required to be the same). Differences between the actual experience of the schemes and the actuarial assumptions made are normally spread over the expected remaining service lives of the current employees in the schemes after making suitable allowances for future withdrawals.

Under U.K. GAAP, FRS 17 “Retirement Benefits”, which sets out the accounting treatment for defined benefit pension schemes, is mandatory for accounting periods beginning on or after 1 January 2005 and therefore the first financial statements prepared in accordance with FRS 17 will be for the year ending 31 March 2006. However, there have been transitional disclosures required in the intervening period. It replaces SSAP 24.

FRS 17 requires all assets to be measured at fair value while scheme liabilities are measured using the projected unit method and are discounted at the current rate of return on a high quality corporate bond of equivalent term and currency to the liability. Full actuarial valuations are required at intervals not exceeding three years and

should be updated at each balance sheet date. Any actuarial gains or losses are recognised immediately in the statement of total recognised gains and losses.

Under U.S. GAAP, defined benefit pension costs, assets and liabilities are recognised in accordance with SFAS 87 “Employers’ Accounting for Pensions” (“SFAS 87”). The method of valuation of defined benefit plan assets and liabilities is similar to U.K. GAAP, but an annual actuarial valuation is required. Actuarial gains and losses may be recognised immediately or amortised over the remaining working lives of participating employees. At a minimum a net gain/loss in excess of 10% of the greater of projected benefit obligation or fair value of plan assets at the beginning of the year must be amortised as a component of net periodic pension cost. A minimum liability must be recognised equal to the amount by which a plan is under funded (ignoring projected future salary increases). SFAS 132R “Employers’ Disclosures about Pensions and other Post Retirement Benefits” is effective beginning the fiscal year ended 31 March 2005 and establishes additional disclosure requirements for pension plans and other post retirement benefit plans.

### **Restructuring costs**

Under U.K. GAAP, provisions including restructuring costs are recognised in accordance with FRS 12 “Provisions, Contingent Liabilities and Contingent Assets” (“FRS 12”), when an entity has a present obligation (legal or constructive) as a result of a past event, when it is probable that a transfer of economic benefit will be required to settle the obligation and a reliable estimate of the obligation can be made. Where that obligation arises as a result of restructuring, it is only acceptable to make a provision for restructuring costs when an obligating event has arisen. Such an event would be the announcement of a restructuring plan generating a valid expectation that the entity will carry out the restructuring.

Under U.S. GAAP, requirements for recording provisions are more stringent than those under U.K. GAAP. Restructuring provisions for exit or disposal activities initiated prior to 31 December 2002 are recorded, in accordance with EITF 94-3 “Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)” (“EITF 94-3”). For plans in existence at 31 December 2002, a liability for the contractual obligation from termination benefit is recorded when probable in accordance with FAS 112 “Employers’ Accounting for Post employment Benefits, an amendment of FAS statement No.5 and 43”. SFAS 146 “Accounting for Costs Associated with Exit or Disposal Activities” (“SFAS 146”) addresses financial accounting and reporting for costs associated with exit or disposal activities and applies to exit or disposal activities initiated after 31 December 2002. SFAS 146 highlights specific recognition and measurement of liabilities criteria that differ in certain respects to those of U.K. GAAP; specifically SFAS 146 requires that certain restructuring costs be recognised when incurred, not upon commitment to a restructuring plan as allowed under U.K. GAAP. Restructuring provisions recorded in connection with a business combination are accounted for in accordance EITF 95-3 “Recognition of Liabilities in Connection with a Purchase Business Combination”.

### **Employee stock-based compensation**

The AWG Group Sharesave Scheme and Executive Share Option Scheme grant options to the employees and executives of Anglian Water in relation to the shares of Anglian Water’s ultimate parent, AWG . AWG does not recharge any costs relating to compensation under these Schemes to Anglian Water. Therefore, under U.K. GAAP, Anglian Water does not recognise any compensation cost under the AWG Group Sharesave Scheme and Executive Share Options Scheme.

Under U.S. GAAP, stock-based employee compensation is accounted for under either APB 25 “Accounting for Stock Issued to Employees” (“APB 25”) or SFAS 123 “Accounting for Stock Based Compensation” (“SFAS 123”). The cost of options granted to employees is recognised over the period to which the employee’s service relates (vesting period) under either the intrinsic value method of APB 25 or the fair value method of SFAS 123. Under the intrinsic value method of APB 25, the measurement date is the date at which both the number of shares to be received and option price are known. Under the fair value method of SFAS 123, the fair value of stock options is typically determined and fixed at grant date.

Under SFAS 123, compensation expense is measured at the grant date based on the fair value of the award and is recognised over the service period, which is usually the vesting period. Under APB 25, compensation expense is the excess, if any, of the quoted market price of the stock at measurement date over the amount an employee must pay to acquire the stock. Fixed stock option plans where the exercise price equals the quoted market price at the date of grant, have no intrinsic value, and under APB 25, no compensation expense is recognised for them. Compensation expense is recognised for other types of stock-based compensation plans under APB 25, including plans with variable, usually performance-based, features. Companies that account for compensation expense

under APB 25 are required to make pro forma disclosures of net income and, if presented, earnings per share, to explain the effects as if accounting under SFAS 123 had been applied.

### **National Insurance Contributions on Share Options**

Share options granted subsequent to 5 April 1999 under approved schemes are subject to employers' and employees' national insurance ("NIC") on the gain made on the exercise of such options by U.K. employees. Under U.K. GAAP, the NIC payable on the difference between the exercise price of the options outstanding and the current market value is calculated and spread over the period up to the date of exercise of the options.

Under U.S. GAAP, the liability for any employee payroll taxes on share options are only recognised when the event triggering the measurement and payment of the tax to the taxing authority occurs, generally the exercise date.

### **Deferred taxation**

U.K. GAAP requires full provision to be made for deferred tax assets and liabilities that arise from timing differences between the recognition of gains and losses in the financial statements and their recognition in the tax computation. Deferred taxation is not provided in respect of taxable timing differences arising from the sale of fixed assets unless it is unlikely that the gain on sale will be rolled over to new assets. The deferred tax balances are calculated using enacted or substantially enacted rates and are discounted using the post tax yields to maturity on government bonds with similar maturity dates. Deferred tax assets are recognised only to the extent that it is considered more likely than not that there will be suitable taxable profits from which the underlying timing differences can be deducted.

Under U.S. GAAP, deferred taxation is provided on all temporary differences between the financial statements carrying amounts of all existing assets and liabilities and their respective tax bases. Deferred taxation is provided at the applicable enacted statutory tax rate expected to apply to taxable income in the periods in which the deferred tax asset or liability is expected to be settled or realised at the reporting date, subject to a valuation allowance to reduce deferred tax assets to the amount which "more likely than not" will be realised in the future tax returns. In addition, U.S. GAAP does not allow discounting of deferred tax assets and liabilities.

### **Debt issue costs**

Debt issue costs are, under both U.K. GAAP and U.S. GAAP, amortised to earnings using the effective yield method. However, under U.K. GAAP debt issue costs are offset against the related debt while under U.S. GAAP such costs are capitalised and reported as deferred charges.

### **Derivative financial instruments**

Under U.K. GAAP, the interest differentials on interest rate swaps treated as hedges are taken to net interest payable in the profit and loss account. Transactions in foreign currencies, if hedged forward, are recorded at the rate of exchange under the related currency contract. Derivatives are recorded at cost or proceeds received and any premiums or fees are amortised over the life of the instrument. Under U.K. GAAP, Financial Reporting Standard No. 13 "Derivatives and Other Financial Instruments: Disclosures" ("FRS 13") additional disclosure is required for financial instruments for all entities that have any of their capital instruments listed or publicly traded on a stock exchange or market.

Under U.S. GAAP, SFAS 133 "Accounting for Derivative Instruments and Hedging Activities", as amended by SFAS 137, SFAS 138 and SFAS 149 ("SFAS 133") requires all derivative financial instruments to be recorded on the balance sheet at their fair value. Changes in the fair value of derivatives are recorded each period in earnings or other comprehensive income (outside earnings) depending on whether a derivative is designated as part of a hedge transaction and, if it is, the type of hedge transaction and whether or not the hedge is effective. Gains and losses on derivative instruments reported in other comprehensive income are reclassified into earnings in the periods in which earnings are affected by the hedge item.

### **Dividends**

Under U.K. GAAP, dividends are provided for in the year in respect of which they are proposed by the Board of Directors for approval of shareholders. These dividends are recorded in the statement of operations as an appropriation of the current year's earnings. U.S. GAAP recognises dividends as a reduction of retained earnings in the accounting period in which they are formally declared and a notice is given to Shareholders.

## **Exceptional items**

Certain events or transactions, because of their size or incidence, are separately classified as ‘exceptional items’ but are included within the calculation of operating profit. Certain gains or losses because of their nature, such as the sale or termination of operations, the fundamental reorganisation of operations or the sale of fixed assets, are presented as non-operating exceptional items and are excluded from the calculation of operating profit.

Exceptional items under U.K. GAAP would not meet the definition of extraordinary items under U.S. GAAP, which requires an event to be both infrequent and unusual. Items classified as an exceptional item in the U.K. GAAP financial statements would be included within operating expenses in a U.S. GAAP presentation, although individual large items may still be separately reported within the determination of operating income.

U.S. GAAP requires the gains or losses from the early extinguishment of debt to be presented separately on the face of the income statement as extraordinary, net of taxes. SFAS 145 “Recession of SFAS 4, 44 and 64 amendment of SFAS 13 and technical corrections” effective for fiscal years beginning after 15 May 2002 removes the provision that early extinguishment of debt is extraordinary. As a result, gains and losses from extinguishment of debt should be classified as extraordinary items only if they meet the criteria in APB 30.

## **Debt Extinguishment**

Under U.K. GAAP, where the life of a debt instrument is shortened, for example through early redemption, or company has the option to redeem, the amortisation of issue costs and any premium on redemption should be accelerated over the remaining period of the shortened term. When it becomes virtually certain that the debt instrument will be redeemed early, the amortisation of deferred debt issue costs is accelerated such that the deferred debt issue costs at the start of the year are amortised over the remaining expected life of the debt instrument.

Under U.S. GAAP, in periods preceding extinguishment, interest expense and other carrying costs of the debt should be recognised in accordance with the terms of the instrument. Deferred debt issue costs would continue to be amortised based on the life of the debt that was assumed when the obligation initially was recorded.

## **Financial Statements Presentation**

### *Disclosures*

The disclosures required under U.S. GAAP are more extensive in certain respects than those required under U.K. GAAP. For example, under U.S. GAAP more detailed disclosures would be included with respect to taxation (details of the components of current and deferred tax expense and deferred tax items, including valuation allowances), segmental reporting and equity (where a statement of changes in shareholders’ equity is required)..

## **Consolidated Balance sheet presentation**

The balance sheet prepared in accordance with U.K. GAAP differs in certain respects from U.S. GAAP. Under U.K. GAAP, current assets are netted against current liabilities in the balance sheet whereas U.S. GAAP requires the separate presentation of total assets and total liabilities. U.K. GAAP requires assets to be presented in ascending order of the liquidity in accordance with the requirements of the Companies Act 1985, whereas under U.S. GAAP assets are presented in descending order of liquidity. In addition, current assets under U.K. GAAP include amounts that fall due after more than one year. Under U.S. GAAP, such assets would be reclassified as non-current assets.

Under U.K. GAAP, indebtedness is presented net of deferred debt issuance costs, while under U.S. GAAP, such deferred costs are classified as a separate asset in the balance sheet with indebtedness being reported on a gross basis

## **Consolidated Statement of Cash Flows**

Under U.K. GAAP, the consolidated cash flow statements are presented in accordance with Financial Reporting Standard No. 1 (revised) “Cash flow statements” (“FRS 1”). Its objectives and principles are similar to U.S. GAAP as set out in SFAS 95 “Statement of Cash Flows” (“SFAS 95”). The principal difference between the standards is in respect of classification. Under FRS 1 (Revised), Anglian Water presents its cash flows for: (a) operating activities; (b) returns on investments and services of finance; (c) taxation; (d) capital expenditure and financial investment; (e) acquisitions and disposals; (f) equity dividends paid; (g) management of liquid resources; and (h) financing. SFAS 95 requires only three categories of cash flow activity: (x) operating activities; (y) investing activities; and (z) financing activities.

Under FRS 1 (Revised), cash includes deposits and overdrafts repayable on demand while movements on short-term investments are included in management of liquid resources. SFAS 95 defines cash and cash equivalents as also including highly liquid short-term investments, with original maturities of three months or less, and excludes overdrafts.

Cash flows arising from taxation and returns on investments and servicing of finance under FRS 1 (Revised) would be included as operating activities under SFAS 95. Cash flows relating to capital expenditure and financial investment and acquisitions and disposals would be included as investing activities under SFAS 95. Equity dividend payments would be included as a financing activity under SFAS 95.

### **Related parties**

Under U.K. GAAP, Anglian Water is exempt from making related party disclosures of transactions and balances with other members of the AWG Group since it is a wholly-owned subsidiary of AWG although disclosures of this nature are contained in the Regulatory Information prepared to comply with Condition F of the Instrument of Appointment.

Under U.S. GAAP, there is no such exemption and, accordingly, related party disclosures are required.

**No attempt has been made to quantify the impact of the above accounting pronouncements or to identify any future differences between UK GAAP and U.S. GAAP that may affect the financial information of Anglian Water.**

## CHAPTER 18

### INDEX OF DEFINED TERMS

The following terms are used throughout this Prospectus:

<b>“Acceleration of Liabilities” or “Acceleration”</b>	means an acceleration of any Secured Liabilities or termination of a commitment (or equivalent action) including: <ul style="list-style-type: none"><li>(a) the delivery of a termination notice from a Finance Lessor or Anglian Water terminating the leasing of any Equipment under a Finance Lease;</li><li>(b) the delivery of a notice by Anglian Water or a Finance Lessor requesting the prepayment of any Rentals under a Finance Lease;</li><li>(c) the early termination of any hedging obligations (whether by reason of an event of default, termination event or other right of early termination) under a Hedging Agreement; or</li><li>(d) the taking of any other steps to recover any payment due in respect of any Secured Liabilities which have matured for repayment and are overdue, by a Secured Creditor or Secured Creditors pursuant to the terms of the applicable Finance Documents and in accordance with the STID;</li></ul>
<b>“Accession Memorandum”</b>	means each memorandum entered into by an additional Secured Creditor pursuant to the STID;
<b>“Account”</b>	means any bank account of any member of the Anglian Water Services Financing Group;
<b>“Account Bank”</b>	means Barclays Bank PLC of Huntingdon, Market Hill PE18 6AE or any successor account bank appointed pursuant to the Account Bank Agreement;
<b>“Account Bank Agreement”</b>	means the account bank agreement dated on or about the Effective Date between, <i>inter alios</i> , the Obligors, the Cash Manager, the Account Bank and the Security Trustee;
<b>“Additional Secured Creditor”</b>	means any person not already a Secured Creditor which becomes a Secured Creditor pursuant to the provisions of the STID;
<b>“Advance”</b>	means any advance or other credit accommodation provided under any Authorised Credit Facility;
<b>“AFC Amounts”</b>	means any amount which constitutes the Annual Finance Charge and which is actually due and payable, calculated in accordance with the CTA;
<b>“Affiliate”</b>	means (other than in any Hedging Agreement when used in relation to a Hedge Counterparty, where “Affiliate” has the meaning given to it in that Hedging Agreement) a Subsidiary or a Holding Company of a person or any other Subsidiary of that Holding Company;
<b>“Agency Agreement”</b>	means the agreement dated 30 July 2002 as supplemented by a supplemental agency agreement dated on or about 23 September 2005 between, <i>inter alios</i> , the Issuer, the

Bond Trustee and the agents referred to therein under which, amongst other things, the Principal Paying Agent is appointed as issuing agent, principal paying agent and agent bank for the purposes of the Programme;

- “AMP3”** means the five-year period commencing on 1 April 2000;
- “AMP4 Period”** means the five-year period commencing on 1 April 2005;
- “Anglian Group”** means AWG and all persons directly or indirectly Controlled by AWG;
- “Anglian Water” and “AWS”** means Anglian Water Services Limited, a United Kingdom incorporated wholly-owned subsidiary of Anglian Water Services Overseas Holdings Ltd which has been appointed a water and sewerage undertaker under the Instrument of Appointment;
- “Anglian Water Business Financial Model”** means the business financial model prepared by Anglian Water and delivered to the Security Trustee from time to time and which, in relation to Trigger Events, must be prepared on the basis of actual figures then in issue from the Director General, rather than from any projected figures that may arise from any pending IDOK application or Competition Commission referral;
- “Anglian Water Change of Control”** means the occurrence of any of the following events or circumstances:
- (a) Anglian Water Services Holdings Ltd ceasing to hold legally and beneficially all rights in 100 per cent. of the issued share capital of, or otherwise ceasing to Control, Anglian Water Services Overseas Holdings Ltd;
  - (b) Anglian Water Services Overseas Holdings Ltd ceasing to hold legally and beneficially all rights in 100 per cent. of the issued share capital of, or otherwise ceasing to Control, Anglian Water; or
  - (c) Anglian Water ceasing to hold legally and beneficially all rights in 100 per cent. of the issued share capital of, or otherwise ceasing to Control, the Issuer;
- “Anglian Water Group”** means Anglian Water and its subsidiary, the Issuer;
- “Anglian Water Loan Notes”** means the loan notes issued by Anglian Water to the Issuer and the rights of the Issuer under certain assigned intercompany loans as more particularly described in Section 7.4.1, *“Financing Structure – Intercompany Loan Arrangements – Anglian Water Loan Notes”*;
- “Anglian Water Services Financing Group” and “AWS Financing Group”** means Anglian Water Services Holdings Ltd, Anglian Water Services Overseas Holdings Ltd, Anglian Water and the Issuer;
- “Anglian Water Services Holdings Ltd” and “AWS Holdings”** means Anglian Water Services Holdings Limited, a United Kingdom incorporated wholly-owned subsidiary of AWG Group Ltd;
- “Anglian Water Services Overseas Holdings Ltd” and “AWS Overseas Holdings”** means Anglian Water Services Overseas Holdings Limited, a Cayman Islands incorporated wholly-owned subsidiary of Anglian Water Services Holdings Ltd;



<b>“Annual Finance Charge”</b>	means, in respect of the Pre-Test Period and thereafter each 12 month period commencing on 1 April in any subsequent year, the aggregate of all interest due or to become due (after taking account of the impact of interest rates on any Hedging Agreements then in place) during that Pre-Test Period or 12 month period, all premia payable to any Financial Guarantor within that Pre-Test Period or 12 month period and the Lease Reserve Amounts and adjusted Lease Reserve Amounts falling due in that Pre-Test Period or 12 month period;
<b>“Applicable Accounting Principles”</b>	means accounting principles, standards and practices generally accepted in the United Kingdom as applied from time to time and making such adjustments (if any) as the directors may consider appropriate arising out of changes to applicable accounting principles or otherwise from time to time;
<b>“Arranger”</b>	means Barclays Bank PLC, as arranger of the Programme;
<b>“Associate”</b>	means any person associated with or in whom any member of the AWG Group or any successor of any of them or any member of any successor group of companies owning or controlling any interest in the Anglian Water Services Financing Group has an interest (whether directly or indirectly);
<b>“Assumptions”</b>	means those assumptions which formed the basis for the Anglian Water Business Financial Model;
<b>“Auditors”</b>	means PricewaterhouseCoopers LLP or such other firm of accountants of international repute as may be appointed by Anglian Water in accordance with the CTA as the Auditors for the Anglian Water Services Financing Group;
<b>“Authorised Credit Facilities”</b>	means any facility or agreement entered into by the Issuer (or in the case of a Finance Lease, Anglian Water) for Class A Debt or Class B Debt as permitted by the terms of the Common Terms Agreement or for the issue of Bond Policies in relation thereto, the providers of which have acceded to the STID and the Common Terms Agreement and includes (without limitation) the Initial Authorised Loan Agreement, the Bridging Facility, the Liquidity Facilities, the Existing Finance Leases, the Anglian Water Loan Notes, the Issuer/Anglian Water Loan Agreement, the Bond Trust Deed, the Existing Bond Trust Deeds, the Bonds, the Existing Hedging Agreements, the Premium Letters, the I&I Agreements and any other document entered into in connection with an Authorised Credit Facility or the transactions in an Authorised Credit Facility;
<b>“Authorised Credit Provider”</b>	means a lender or other provider of credit or financial accommodation under any Authorised Credit Facility and includes each Financial Guarantor for so long as any Bond Policy issued by that Financial Guarantor is outstanding, and each Bondholder;
<b>“Authorised Investments”</b>	means: <ul style="list-style-type: none"> <li>(a) securities issued by the government of the United Kingdom;</li> <li>(b) demand or time deposits, certificates of deposit and short-term unsecured debt obligations, including</li> </ul>

commercial paper, provided that the issuing entity or, if such investment is guaranteed, the guaranteeing entity, is rated the Minimum Short-term Rating;

- (c) any other obligations provided that in each case the relevant investment has the Minimum Short-term Rating and is either denominated in Sterling or (following the date on which the UK becomes a Participating Member State) euro or has been hedged in accordance with the Hedging Policy; or
- (d) any money market funds or equivalent investments which have a rating of at least A+m by S&P or A+ by Fitch or A1 by Moody's, provided that in Anglian Water's reasonable opinion it is able to liquidate such funds on a same day basis without material cost penalties being imposed;

<b>“Authorised Credit Facility Agent”</b>	means Barclays Bank PLC, or any successor thereto in respect of the Authorised Loan Agreement;
<b>“Authorised Credit Facility Arranger”</b>	means Barclays Capital, or any successor thereto in respect of the Authorised Loan Agreement;
<b>“Authorised Credit Providers”</b>	means any party to the Authorised Loan Agreement as lender or a Finance Party;
<b>“Authorised Loan Agreement”</b>	means the bank facility entered into between, <i>inter alios</i> , the Issuer and the Initial Authorised Credit Providers on 25 November 2004;
<b>“Authority”</b>	means the Water Services Regulation Authority, which will replace the DGWS pursuant to the Water Act;
<b>“AW Group”</b>	means the group of companies of AWG Group Ltd and its subsidiaries prior to the introduction of AWG as parent company in 2000;
<b>“AWCT”</b>	means AW Creative Technologies Limited, a wholly-owned subsidiary of AWG;
<b>“AWG”</b>	means AWG plc, a company incorporated under the laws of England and Wales which is admitted to the Official List and to trading on the London Stock Exchange, the holding company of the AWG Group;
<b>“AWG Group”</b>	means AWG and its subsidiaries;
<b>“AWG Group Ltd”</b>	means AWG Group Ltd (formerly Anglian Water Plc), a company incorporated under the laws of England and Wales and formerly listed on the London Stock Exchange, a wholly-owned subsidiary of AWG;
<b>“AWPS”</b>	means the AWG Pension Scheme, a retirement benefit arrangement in which the AWG Group companies participate;
<b>“Base Cash Flows”</b>	means the annual cash flows of the amounts of costs netted off against the amount of receipts and savings in respect of each Relevant Change of Circumstance, Notified Item and relevant disposal of land;
<b>“Bearer Bonds”</b>	means those of the Bonds which are in bearer form;

<b>“Blue Flag”</b>	means an annual award to beaches that meet guideline standards under the Bathing Water Directive and 25 beach management criteria;
<b>“Blue Flag Water Policy”</b>	means the policy of Anglian Water which, amongst other things, aims for 100 per cent. compliance with both the mandatory and guideline coliform standards by 2005;
<b>“Bondholders”</b>	means the holders from time to time of the Bonds;
<b>“Bond Policies”</b>	means the financial guarantee insurance policy issued by a Financial Guarantor in respect of Class A Wrapped Bonds and/or Class B Wrapped Bonds which includes the Initial Bond Policies;
<b>“Bonds”</b>	means the Class A Bonds and the Class B Bonds;
<b>“Bond Trustee”</b>	means Deutsche Trustee Company Limited or any successor trustee appointed pursuant to the Bond Trust Deed and/or the Existing Bond Trust Deeds, for and on behalf of the relevant Bondholders;
<b>“Bond Trust Deed”</b>	means (a) in respect of Bonds issued under the Programme, the Bond Trust Deed dated 30 July 2002 between, <i>inter alios</i> , the Issuer, the Initial Financial Guarantor and the Bond Trustee under which Bonds will, on issue, be constituted and which sets out the terms and conditions on which the Bond Trustee has agreed to act as bond trustee; and (b) in respect of the Existing Bonds, the Existing Bond Trust Deeds (and, in respect of such Bonds issued after the date of this Prospectus, as supplemented by a first supplemental trust deed dated on or about 23 September 2005);
<b>“Bridging Facility”</b>	means the bridge facility made available under the Bridging Facility Agreement;
<b>“Bridging Facility Agent”</b>	means Barclays Bank PLC or any successor thereto;
<b>“Bridging Facility Agreement”</b>	means the bridging facility agreement dated 18 April 2002 between the Issuer, the other Obligors, the Facility Arrangers, the Original Lenders and the Facility Agent (each as defined therein) and which is now cancelled;
<b>“Business”</b>	means Regulated Business and Permitted Non-Statutory Business whether under a Permitted Joint Venture or otherwise as permitted under the Finance Documents;
<b>“Business Day”</b>	means (other than in any Hedging Agreement where “Business Day” has the meaning given to it in that Hedging Agreement): <ul style="list-style-type: none"> <li>(a) in relation to any sum payable in euro, a TARGET Settlement Day and a day on which commercial banks and foreign exchange markets settle payments generally in London and each (if any) additional city or cities specified in the relevant Final Terms;</li> <li>(b) in relation to any sum payable in a currency other than euro, a day on which commercial banks and foreign exchange markets settle payments generally in London, in the principal financial centre of the currency in which such financial indebtedness is</li> </ul>

denominated (which in the case of a payment in US dollars shall be New York) and in each (if any) additional city or cities specified in the relevant Final Terms; and

- (c) in relation to the definition of Lease Calculation Date, a day on which commercial banks and foreign exchange markets settle payments generally in London;

<b>“Calculation Date”</b>	means (other than in any Hedging Agreement where “Calculation Date” has the meaning given to it in that Hedging Agreement), 31 March and 30 September in each year starting on 31 March 2002 or any other calculation date agreed as a result of a change in the financial year end date of any Obligor;
<b>“CAMS”</b>	means Catchment Abstraction Management Strategies, which are part of the Government’s plans to reform water resources planning;
<b>“CAT”</b>	means the Competition Appeal Tribunal of the United Kingdom;
<b>“Capex Contract”</b>	means any agreement pursuant to which Anglian Water outsources any investment, construction works and other capital expenditure;
<b>“Capex Reserve Account”</b>	means the account of Anglian Water titled “Capex Reserve Account” held at the Account Bank and includes any sub-account relating to that account and any replacement account from time to time;
<b>“Capital Maintenance Expenditure”</b>	means investment expenditure incurred (or, in respect of any future period, forecast to be incurred in the Anglian Water Business Financial Model) on maintaining base service levels in the Regulated Business and excluding any investment expenditure relating to increases in capacity or enhancement of service levels, quality or security of supply;
<b>“Cash Expenses”</b>	means the aggregate of all expenses incurred by Anglian Water in any period (excluding depreciation, IRC and interest on Financial Indebtedness);
<b>“Cash Manager”</b>	means Barclays Bank PLC during and after a Standstill Period (except where the Standstill Period is terminated because the Event of Default giving rise to the Standstill is remedied or waived), in its capacity as Cash Manager under the CTA, or any successor Cash Manager, and at all other times Anglian Water;
<b>“CCD”</b>	means expenditure designated under the heading current cost depreciation in the financial projections contained in the supplementary report issued by Ofwat detailing the numbers and assumptions specific to Anglian Water in the DGWS’s most recent Final Determination adjusted as appropriate for any subsequent IDOK and for Out-turn Inflation;
<b>“Chief Inspector of Drinking Water”</b>	means the person from time to time designated as Chief Inspector of Drinking Water by the Secretary of State pursuant to s.86 of the WIA, as amended by s.57 of the Water Act;

<b>“Class”</b>	means each class of Bonds, the available Classes of Bonds being Class A Wrapped Bonds, Class A Unwrapped Bonds, Class B Wrapped Bonds and Class B Unwrapped Bonds;
<b>“Class A Average PMICR”</b>	means the sum of the ratios of Net Cash Flow less the greater of (a) the aggregate of CCD and IRC and (b) Capital Maintenance Expenditure to Class A Debt Interest for each of the Test Periods comprised in a Rolling Average Period divided by 3;
<b>“Class A Bonds”</b>	means the Class A Wrapped Bonds and the Class A Unwrapped Bonds;
<b>“Class A Debt”</b>	<p>means any financial accommodation that is, for the purposes of the STID, to be treated as Class A Debt and includes as at the Effective Date all debt outstanding under:</p> <ul style="list-style-type: none"> <li>(a) the Class A Wrapped Bonds and the Class A Unwrapped Bonds (if any) issued by the Issuer on or after the Effective Date;</li> <li>(b) the Existing Bonds and the USPP 2001 Bonds which the Issuer will assume liability for on the Effective Date;</li> <li>(c) the Initial Authorised Loan Agreement;</li> <li>(d) the Existing Finance Leases;</li> <li>(e) the Existing Hedging Agreements;</li> <li>(f) tranche A1 and tranche B and the Class A portion of tranche A2 of the Bridging Facility;</li> <li>(g) the Debt Service Reserve Liquidity Facilities;</li> <li>(h) the O&amp;M Reserve Facility;</li> <li>(i) the MBIA Premium Letter; and</li> <li>(j) the first I&amp;I Agreement;</li> </ul>
<b>“Class A Debt Instructing Group” or “Class A DIG”</b>	<p>means a group of representatives (each a “<b>Class A DIG Representative</b>”) of Qualifying Class A Debt, comprising of:</p> <ul style="list-style-type: none"> <li>(a) in respect of each Series of Class A Wrapped Bonds (if no FG Event of Default has occurred and is continuing), the Financial Guarantor;</li> <li>(b) in respect of each Series of Class A Wrapped Bonds (after an FG Event of Default has occurred and is continuing in respect of the Financial Guarantor of those Bonds) and each Series of Class A Unwrapped Bonds (other than USPP Bonds), the Bond Trustee;</li> <li>(c) in respect of Class A USPP Bonds (i) prior to the occurrence of an Event of Default, any USPP Bondholder who has outstanding to it or any of its affiliates more than US\$70,000,000 of Class A USPP Bonds or (ii) after an Event of Default has occurred and is continuing, any USPP Bondholder;</li> </ul>

- (d) in respect of tranche A1 and tranche B and the Class A portion of tranche A2 of the Bridging Facility, the Bridging Facility Agent;
- (e) in respect of the Initial Authorised Loan Agreement, the Initial Authorised Credit Facility Agent;
- (f) in respect of any Existing Finance Leases, the relevant Finance Lessor; and
- (g) in respect of any other Secured Liabilities of the type referred to in paragraphs (a) to (f) above or (with the approval of the Majority Creditors) other types of Secured Liabilities that rank pari passu with all other Class A Debt, the relevant representative appointed under the terms of the relevant Finance Document and named in the relevant Accession Memorandum as the Class A DIG Representative,

each of which provides an appropriate indemnity to the Security Trustee each time it votes irrespective of whether it is a Majority Creditor;

**“Class A Debt Interest”**

means, in relation to any Test Period, and without double counting an amount equal to the aggregate of all interest paid, due but unpaid or in respect of forward looking ratios payable on the Issuer’s and/or Anglian Water’s obligations under or in connection with all Class A Debt, all premia paid, due but unpaid or in respect of forward looking ratios, payable, to any Financial Guarantor of Class A Debt and adjusted Lease Reserve Amounts or Lease Reserve Amounts paid, due but unpaid or in respect of forward looking ratios, payable on the Issuer’s and/or Anglian Water’s obligations under and in connection with all Class A Debt in each case during such Test Period (after taking account of the impact on interest rates of all related Hedging Agreements then in force) (excluding all indexation of principal to the extent it has been included in such interest or other amounts) and excluding amortisation of the costs of issue of any Class A Debt within such Test Period and all other costs incurred in connection with the raising of such Class A Debt less all interest received or in respect of forward looking ratios receivable by any member of the Anglian Water Services Financing Group from a third party during such period;

**“Class A Debt Service Reserve Account” or “Class A DSRA”**

means the account of the Issuer titled “Class A Debt Service Reserve Account” held at the Account Bank and includes any sub-account relating to that account and any replacement account from time to time;

**“Class A Debt Provider”**

means a provider of, or Financial Guarantor of, Class A Debt;

**“Class A ICR”**

means the ratio of Net Cash Flow for each Test Period to Class A Debt Interest for each of the same Test Periods;

**“Class A Net Indebtedness”**

means, as at any date, all the Issuer’s and Anglian Water’s nominal debt outstanding under and in connection with any Class A Debt (other than pursuant to tranche B of the Initial Authorised Loan Agreement) including all indexation accrued on any such liabilities which are indexed together with any interest due but unpaid (after taking into account the effect of

all Interest Rate Hedging Agreements then in force) and less the value of all Authorised Investments and other amounts standing to the credit of any Account other than the Customer Payment Account or the Distributions Account) (where such debt is denominated other than in Sterling, the nominal amount outstanding will be calculated: (i) in respect of debt with associated Currency Hedging Agreements, by reference to the applicable hedge rates; or (ii) in respect of debt with no associated Currency Hedging Agreements, by reference to the Exchange Rate);

<b>“Class A PMICR”</b>	means the ratio of Net Cash Flow less the greater of (a) the aggregate of CCD and IRC and (b) Capital Maintenance Expenditure for each Test Period to Class A Debt Interest for the same Test Period;
<b>“Class A RAR”</b>	means the ratio of Class A Net Indebtedness to RAV;
<b>“Class A Unwrapped Bonds”</b>	means the Class A Bonds that do not have the benefit of a guarantee from a Financial Guarantor, which includes the Transferred USPP Bonds and some of the Existing Bonds;
<b>“Class A Unwrapped Debt”</b>	means the Class A Debt that does not have the benefit of a guarantee from a Financial Guarantor;
<b>“Class A USPP Bonds”</b>	means USPP Bonds which are also Class A Bonds;
<b>“Class A Wrapped Bonds”</b>	means the Class A Bonds that have the benefit of a guarantee from a Financial Guarantor, which includes some of the Existing Bonds;
<b>“Class A Wrapped Debt”</b>	means Class A Debt that has the benefit of a guarantee from a Financial Guarantor;
<b>“Class B Bonds”</b>	means the Class B Wrapped Bonds and the Class B Unwrapped Bonds;
<b>“Class B Debt”</b>	means any financial accommodation that is, for the purposes of the STID, to be treated as Class B Debt and includes as at the Effective Date all debt outstanding under:  (a) the Class B Bonds; and  (b) the Class B portion of tranche A2 of the Bridging Facility;
<b>“Class B Debt Instructing Group” or “Class B DIG”</b>	means a group of representatives (each a <b>“Class B DIG Representative”</b> ) of Qualifying Class B Debt, comprising of:  (a) in respect of each series of Class B Wrapped Bonds (if no FG Event of Default has occurred and is continuing), the Financial Guarantor;  (b) in respect of each Series of Class B Wrapped Bonds (after an FG Event of Default, has occurred and is continuing in respect of the Financial Guarantor of those Bonds) and each Series of Class B Unwrapped Bonds, the Bond Trustee;  (c) in respect of the Class B Debt portion of tranche A2 of the Bridging Facility, the Bridging Facility Agent; and

- (d) in respect of any other Secured Liabilities of the type referred to in paragraphs (a) to (c) above or (with the approval of the Majority Creditors) other types of Secured Liabilities that rank *pari passu* with all other Class B Debt, the relevant representative appointed under the terms of the relevant Finance Document and named in relevant Accession Memorandum, as the Class B DIG Representative,

each of which provides an appropriate indemnity to the Security Trustee each time it votes irrespective of whether it is a Majority Creditor;

<b>“Class B Debt Service Reserve Account” or “Class B DSRA”</b>	means the account of the Issuer titled “Class B Debt Service Reserve Account” held at the Account Bank and includes any sub-account relating to that account and any replacement account from time to time;
<b>“Class B Debt Provider”</b>	means any provider of, or Financial Guarantor of, Class B Debt;
<b>“Class B Unwrapped Bonds”</b>	means the Class B Bonds that do not have the benefit of a guarantee from a Financial Guarantor;
<b>“Class B Unwrapped Debt”</b>	means Class B Debt that does not have the benefit of a guarantee from a Financial Guarantor;
<b>“Class B USPP Bonds”</b>	means Class B Bonds which are also USPP Bonds;
<b>“Class B Wrapped Bonds”</b>	means the Class B Bonds that have the benefit of a guarantee from a Financial Guarantor;
<b>“Class B Wrapped Debt”</b>	means Class B Debt that has the benefit of a guarantee from a Financial Guarantor;
<b>“Clearstream, Luxembourg”</b>	means Clearstream Banking, société anonyme;
<b>“Combined Contract”</b>	means any agreement pursuant to which Anglian Water sub-contracts, tenders or outsources both investment or construction works or other capital expenditure as well as the day to day operation of its assets and service delivery or any maintenance expenditure;
<b>“Common Terms Agreement” or “CTA”</b>	means the Common Terms Agreement dated 30 July 2002 between the Obligors and, <i>inter alios</i> , the Security Trustee, which contains certain representations and covenants of the Obligors and Events of Default;
<b>“Companies Act”</b>	means the United Kingdom Companies Act 1985, as amended from time to time;
<b>“Company”</b>	means Anglian Water;
<b>“Company Collective”</b>	means the recognised body of employee, trade union and management representatives for collective bargaining in determining the terms and conditions of employment for Anglian Water employees and consultation on issues affecting those employees, for example, redundancies and TUPE transfers;
<b>“Compensation Account”</b>	means the account of Anglian Water entitled “Compensation Account” held at the Account Bank and includes any



	sub-account relating to that account and any replacement account from time to time;
<b>“Competition Act”</b>	means the United Kingdom Competition Act 1998;
<b>“Competition Commission”</b>	means the Competition Commission in the United Kingdom;
<b>“Conditions”</b>	means the terms and conditions of the Bonds set out in the Bond Trust Deed as may from time to time be amended, varied or supplemented in the manner permitted under the STID;
<b>“Construction Output Price Index”</b>	means the index issued by the Department of Trade and Industry, varied from time to time, relating to price levels of new build construction based on a combination of logged values of tender price indices, labour and materials cost indices and on the value of new construction orders in the United Kingdom;
<b>“Contractors”</b>	means any person (being either a single entity or joint venture) that is a counterparty to an Outsourcing Agreement or Capex Contract or Combined Contract;
<b>“Control”</b>	of one person by another person means that the other (whether directly or indirectly and whether by the ownership of share capital, the possession of voting power, contract or otherwise) and whether acting alone or in concert with another or others has the power to appoint and/or remove the majority of the members of the governing body of that person or otherwise controls or has the power to control the affairs and policies of that person (and references to <b>“Controlled”</b> and <b>“Controlling”</b> shall be construed accordingly);
<b>“Council”</b>	means the Ofwat National Customer Council;
<b>“Coupon”</b>	means an interest coupon appertaining to a definitive Bearer Bond (other than a Zero Coupon Bond);
<b>“Couponholders”</b>	means the several persons who are for the time being holders of the Coupons and includes, where applicable, the Talonholders;
<b>“Court”</b>	means the High Court of England and Wales;
<b>“CP Document”</b>	means the agreement entitled “Conditions Precedent Agreement” dated 30 July 2002 and entered into, <i>inter alios</i> , between the Obligors, the Bond Trustee and the Security Trustee;
<b>“CSCs”</b>	means regional customer service committees established by the DGWS;
<b>“Currency Hedging Agreement”</b>	means any Hedging Agreement with a Hedge Counterparty in respect of a currency exchange transaction;
<b>“Customer Payment Account”</b>	means the account of Anglian Water titled “Customer Payment Account” held at the Account Bank and includes any sub-account relating to that account and any replacement account from time to time;

<b>“Customer Payment Account Required Balance”</b>	means, at any time during a Financial Year, the amount calculated in accordance with the following formula:
	$\frac{\text{CRA}}{12} \times m$
	where CRA means, in respect of such Financial Year, the aggregate Customer Rebates declared, and m means the number of accounting months unexpired in such Financial Year;
<b>“Customer Rebates”</b>	means, in respect of any Financial Year, an amount equal to the difference between the total revenue that is projected by Anglian Water to be raised during such Financial Year on the basis of the announced charges and the revenue that would have accrued if Anglian Water had established prices at the full price cap available to it under the Instrument of Appointment;
<b>“Date Prior”</b>	means, at any time, the date which is one day before the next Periodic Review Effective Date;
<b>“Dealers”</b>	means Barclays Bank PLC and any other entity which the Issuer and the Obligors may appoint as a Dealer and notice of whose appointment has been given to the Principal Paying Agent and the Bond Trustee by the Issuer in accordance with the provisions of the Programme Agreement but excluding any entity whose appointment has been terminated in accordance with the provisions of the Programme Agreement and notice of such termination has been given to the Principal Paying Agent and the Bond Trustee by the Issuer in accordance with the provisions of the Programme Agreement and references to a <b>“relevant Dealer”</b> or the <b>“relevant Dealer(s)”</b> mean, in relation to any Tranche or Series of Bonds, the Dealer or Dealers with whom the Issuer has agreed the issue of the Bonds of such Tranche or Series and <b>“Dealer”</b> means any one of them;
<b>“Debt Service Payment Account”</b>	the account of the Issuer entitled the “Debt Service Payment Account” held at the Account Bank and includes any sub-account relating to that account and any replacement account from time to time;
<b>“Debt Service Reserve Account”</b>	means any or both of the Class A Debt Service Reserve Account and/or the Class B Debt Service Reserve Account;
<b>“Debt Service Reserve Liquidity Facility”</b>	means a debt service reserve liquidity facility made available under a Liquidity Facility Agreement;
<b>“Debt Service Reserve Liquidity Facility Agreement”</b>	means any agreement establishing a Debt Service Reserve Liquidity Facility as more particularly described in Section 7.9.4, <i>“Financing Structure – Additional Resources Available – The Liquidity Facilities”</i> ;
<b>“Debt Service Reserve Liquidity Facility Provider”</b>	means Barclays Bank PLC, HSBC Bank plc or the Royal Bank of Scotland plc or any other provider of Debt Service Liquidity Facilities;
<b>“Default”</b>	means: <ul style="list-style-type: none"> <li>(a) an Event of Default;</li> </ul>

	(b) a Trigger Event; or
	(c) a Potential Event of Default;
<b>“Default Situation”</b>	means any period during which there subsists:
	(a) a Standstill Period; or
	(b) an Event of Default;
<b>“Definitive IAI Registered Bond”</b>	means a Registered Bond sold to an Institutional Accredited Investor pursuant to Section 4(2) under the Securities Act;
<b>“DEFRA”</b>	means the Department of the Environment, Food and Rural Affairs in the United Kingdom;
<b>“DETR”</b>	means the Department of the Environment, Transport and the Regions which had responsibility for the Environment prior to DEFRA;
<b>“DGWS” or “Director General”</b>	means the Director General of Water Services in England and Wales;
<b>“DIG Directions Request”</b>	means a written notice of each DIG Proposal sent by the Security Trustee to the relevant DIG Representatives pursuant to the STID;
<b>“DIG Proposal”</b>	means a proposal pursuant to the STID requiring a Majority Creditor decision only;
<b>“DIG Representatives”</b>	means the Class A DIG Representatives or the Class B DIG Representatives, as the context requires and <b>“DIG Representatives”</b> means each of them;
<b>“Directors”</b>	means the board of directors for the time being of the Issuer or as the case may be the relevant Obligor;
<b>“Discharge Date”</b>	means the date on which all obligations of the Issuer under the Finance Documents have been irrevocably satisfied in full and no further obligations are capable of arising under the Finance Documents;
<b>“Distribution”</b>	means:
	(a) any payments (including, without limitation, any payments of distributions, dividends (including any Special Distribution), bonus issues, return of capital, fees, interest, principal or other accounts whatsoever) (by way of loan or repayment of any loan or otherwise) (in cash or in kind) to any member of the AWG Group or any successor entity having an interest in Anglian Water Services Holdings Ltd or any Associate or Affiliate of any such person other than:
	(i) payments made to such persons pursuant to arrangements entered into on <i>bona fide</i> arm’s length terms in the ordinary and usual course of trading to the extent that the aggregate of all such payments does not exceed £5,000,000 (indexed) in any consecutive twelve month period; or

- (ii) any payments made to such persons pursuant to any Outsourcing Agreement and/or Capex Contracts entered into in compliance with the Outsourcing Policy; or
- (iii) payments made to such persons pursuant to arrangements entered into on terms that are not *bona fide* and arm's length in the ordinary and usual course of trading to the extent that the aggregate of all such payments does not exceed £500,000 (indexed) in any consecutive twelve month period; or
- (iv) a UK Holdco Debt Service Distribution; or
- (b) payments made in respect of any Financial Indebtedness falling within paragraph (f) of the definition of Permitted Financial Indebtedness;

<b>“Distributions Account”</b>	means the account of Anglian Water titled “Anglian Water Distributions Account” held at the Account Bank and includes any sub-account relating to that account and any replacement account from time to time;
<b>“DTC”</b>	means The Depository Trust Company of 55 Water Street, New York, NY 10041, United States of America;
<b>“DWI”</b>	means the Drinking Water Inspectorate in the United Kingdom, including its successor office or body;
<b>“EA”</b>	means the UK Environment Agency;
<b>“Early Redemption Amount”</b>	means for the purposes of the USPP 2001 Bonds, the principal and Make-Whole Amount (if any), but excluding any accrued interest payable, to the Bondholder on redemption of a USPP 2001 Bond as a result of an Early Redemption Event occurring and in relation to any other Bonds, as defined in the Conditions relating to such Bonds;
<b>“Early Redemption Event”</b>	means a notice is given pursuant to Clause 8.3(a)A of the Note Purchase Agreement;
<b>“Early Redemption Shortfall”</b>	means a time when the aggregate Early Redemption Amount due and payable exceeds the amount available for drawing under the Bridging Facility to pay Early Redemption Amounts;
<b>“Effective Date”</b>	means 30 July 2002 being the date on which the conditions precedent contained in the CP Document were fulfilled or waived in accordance with the CP Document;
<b>“Emergency”</b>	means the disruption of the normal service of the provision of water or waste water services which is treated as an emergency under Anglian Water's policies, standards and procedures for emergency planning manual (EMPROC) (as amended from time to time);
<b>“Emergency Instruction Notice”</b>	means a notice as set out in Section 7.3.9 “ <i>Financing Structure – Intercreditor Arrangements – Emergency Instruction Notice</i> ”;
<b>“EIB”</b>	means the European Investment Bank;

<b>“EIN Signatories”</b>	has the meaning as set out in Section 7.3.9 <i>“Financing Structure – Intercreditor Arrangements – Emergency Instruction Notice”</i> ;
<b>“ELL”</b>	means the annual Economic Level of Leakage suffered by Anglian Water;
<b>“Enforcement Action”</b>	means any step (other than the exercise of any rights of inspection of any asset or other immaterial actions taken under any Finance Lease) that a Secured Creditor is entitled to take to enforce its rights against an Obligor under a Finance Document following the occurrence of an Event of Default including, without limitation, the declaration of an Event of Default or an Early Redemption Event, the institution of proceedings, the making of a demand for payment under a guarantee, the making of a demand for cash collateral under a guarantee or the Acceleration of Liabilities (other than a Permitted Lease Termination, a Permitted Hedge Termination or a Permitted Acceleration) by a Secured Creditor or Secured Creditors pursuant to the terms of the applicable Finance Documents;
<b>“Enforcement Notice”</b>	means a notice in writing from the Security Trustee to the Issuer and/or Anglian Water specifying that all or any of the Secured Liabilities have or has become immediately enforceable;
<b>“Enforcement Order”</b>	means an enforcement order, a final enforcement order or a provisional enforcement order, each as referred to and defined in the WIA;
<b>“Enterprise Act”</b>	means the Enterprise Act 2002 which received Royal Assent on 7 November 2002;
<b>“Entrenched Rights”</b>	means the rights of the Secured Creditors set out in Section 7.3.19, <i>“Financing Structure – Intercreditor Arrangements – Entrenched Rights”</i> ;
<b>“EPA 1990”</b>	means the Environmental Protection Act 1990;
<b>“Equipment”</b>	means, in relation to a Finance Lease, any items of equipment, plant and/or machinery, system, asset, software licence, intellectual property right, software and any other item leased under that Finance Lease;
<b>“Equivalent Amount”</b>	means the amount in question expressed in the terms of pounds sterling, calculated on the basis of the Exchange Rate;
<b>“EU”</b>	means the European Union;
<b>“Euroclear”</b>	means Euroclear Bank S.A./N.V. as operator of the Euroclear System;
<b>“Event of Default”</b>	means (other than in any Hedging Agreement when used in relation to a Hedge Counterparty, where “Event of Default” has the meaning given to it in that Hedging Agreement) an event specified as such in Schedule 7 of the Common Terms Agreement, as more particularly described under Section 7.5.10, <i>“Financing Structure – Common Terms Agreement – Events of Default”</i> ;

<b>“Exchange Agent”</b>	means Deutsche Bank Trust Company Americas as exchange agent to the Issuer in respect of Registered Bonds;
<b>“Exchange Rate”</b>	<p>means the spot rate at which the relevant currency is converted to pounds sterling as quoted by the Agent Bank as at 11.00 a.m:</p> <p>(a) for the purposes of Clause 9.3 (Notice to Secured Creditors of STID Proposal) and Clause 9.6 (DIG Directions Request) of the STID, respectively, on the date that the STID Proposal or DIG Proposal (as applicable) is dated; and</p> <p>(b) in any other case, on the date as of which calculation of the Equivalent Amount of the Outstanding Principal Amount is required,</p> <p>and, in each case, as notified by the Agent Bank to the Security Trustee;</p>
<b>“Existing Agency Agreements”</b>	means each of those agency agreements in respect of the Existing Bonds as the same shall have been amended on the Effective Date;
<b>“Existing Bonds”</b>	<p>means such of the following Bonds issued by AWG Group Ltd pursuant to the Existing Bond Trust Deeds for which the Issuer assumed liability on the Effective Date:</p> <p>(a) £150,000,000 8.25 per cent. bonds due 2006;</p> <p>(b) £100,000,000 5½ per cent. index-linked loan stock 2008;</p> <p>(c) £100,000,000 12 per cent. bonds 2014;</p> <p>(d) £150,000,000 3.875 per cent. index-linked guaranteed notes due 2020;</p> <p>(e) £200,000,000 6.625 per cent. guaranteed bonds due 2023;</p> <p>(f) £200,000,000 6.375 per cent. guaranteed bonds due 2029; and</p> <p>(g) €350,000,000 5.375 per cent. bonds due 2009.</p> <p>With regard to the assumption of liability by the Issuer of the Existing Bonds on the Effective Date, listing particulars were prepared and submitted to the UK Listing Authority for approval prior to the Effective Date.</p>
<b>“Existing Bond Trust Deeds”</b>	<p>means the bond trust deeds in relation to:</p> <p>(a) £100,000,000 5½ per cent. index-linked loan stock 2008 dated 4 July 1990, between AWG Group Ltd as issuer, Anglian Water as guarantor and Royal Exchange Trust Company Limited as trustee;</p> <p>(b) £100,000,000 12 per cent. bonds 2014 dated 7 January 1991, between AWG Group Ltd as issuer, Anglian Water as guarantor and Sun Alliance Trust Company Limited as trustee;</p>

- (c) £150,000,000 8.25 per cent. bonds due 2006 dated 29 November 1996, between AWG Group Ltd as issuer and Royal Exchange Trust Company Limited as trustee;
- (d) £200,000,000 6.625 per cent. guaranteed bonds due 2023 dated 21 August 1998, between AWG Group Ltd as issuer, Anglian Water as guarantor and Royal Exchange Trust Company Limited as trustee;
- (e) £200,000,000 6.375 per cent. guaranteed bonds due 2029 dated 15 January 1999, between AWG Group Ltd as issuer, Anglian Water as guarantor and Royal Exchange Trust Company Limited as trustee;
- (f) €350,000,000 5.375 per cent. bonds due 2009 dated 2 July 1999, between AWG Group Ltd as issuer and Royal Exchange Trust Company Limited as trustee; and
- (g) €1,500,000,000 MTN Programme dated 22 March 2000, between AWG Group Ltd as issuer, Anglian Water as guarantor and IRG Trustees Limited as trustee, pursuant to which £150,000,000 3.875 per cent. index-linked guaranteed notes due 2020 were issued on 28 April 2000,

as were amended pursuant to a consent solicitation on the Effective Date;

**“Existing Finance Leases”**

means the leases between Anglian Water and the Existing Finance Lessors and which were entered into prior to the Effective Date and each as amended supplemented, assigned and novated prior to the Effective Date, and each an **“Existing Finance Lease”**;

**“Existing Finance Lessors”**

means each of Mercantile Leasing Company (No. 132) Limited, D-LAF Limited or Moon Leasing Limited in its capacity as a general partner of Brahms Leasing Limited Partnership, Deutsche Bank AG, London Branch, CSC Computer Sciences Limited and Barclays Technology Finance Limited, who lease or agree to lease Equipment to Anglian Water, under the terms of the Existing Finance Leases, including any of their successors or assigns and each an **“Existing Finance Lessor”**;

**“Existing Framework Agreements”**

means the framework agreements between Anglian Water and Contractors entered into prior to the Effective Date under which Anglian Water subcontracts, tenders and outsources its operation and maintenance expenditure and/or construction works and other capital expenditure;

**“Existing Hedge Counterparties”**

means Barclays Bank PLC, Citibank, N.A., London Branch, Deutsche Bank AG, London Branch, Dresdner Bank AG, HSBC Bank plc and The Royal Bank of Scotland plc including their successors and assigns;

**“Existing Hedging Agreements”**

means the Treasury Transactions entered into by the Issuer and the Existing Hedge Counterparties dated on or about the Effective Date or any such agreement entered into by Anglian Water or AWG Group Ltd and one or more of the Existing

Hedge Counterparties prior to the Effective Date and novated to the Issuer on or before the Effective Date;

**“Existing Joint Venture”**

means:

- (a) a joint venture called “AB Water” entered into between Anglian Water and Persimmon Homes (formerly Beazer Homes) for effluent recycling;
- (b) a joint venture called “BREG” (Bio-solids Reduction and Energy Generation Plant) entered into between Anglian Water and TXU Europe Power Ltd. for the design, development, construction and operation of plants to generate heat and electricity in a combined cycle power station from natural gas and gasified sewage sludge;
- (c) a joint venture called “Logica” entered into between Anglian Water and Logica UK Ltd. for the development, supply and support of telemetry systems;
- (d) a joint venture called “ABB Kent” entered into between Anglian Water and ABB Metering Limited to develop an automatic meter reading system;
- (e) a joint venture called “Ardleigh Reservoir” pursuant to the Ardleigh Reservoir Order 1967; and
- (f) any Existing Framework Agreements existing at the Effective Date,

details of which have been provided to the Security Trustee and the Initial Financial Guarantor;

**“Extended Outsourcing Agreements”**

means:

- (i) the agreement entitled “Computer Network (PA no. EPAF)” between CSC and Anglian Water which has a PA end date of 31 October 2005;
- (ii) the agreement entitled “Development Framework Agreement (PA no.01/27)” between Logica and Anglian Water which has a PA end date of 31 October 2005; and
- (iii) the agreement entitled “Fleet Maintenance (PA no. 00/75)” between PowerMarque Ltd and Anglian Water which has a PA end date of 31 March 2004,

copies of which have been provided to each Financial Guarantor and the Security Trustee;

**“Facility Agent”**

means any facility agent under any Authorised Credit Facility;

**“FG Event of Default”**

means in relation to the Initial Financial Guarantor:

- (a) any Insured Amount which is Due for Payment (each as defined under the relevant Bond Policy) is unpaid by reason of non-payment by the Issuer and is not paid by such Financial Guarantor on the date stipulated in the relevant Bond Policy;



- (b) such Financial Guarantor disclaims, disaffirms, repudiates and/or challenges the validity of any of its obligations under the relevant Bond Policy or seeks to do so;
- (c) such Financial Guarantor:
  - (i) presents any petition, commences any case or takes any proceedings for the winding-up or the appointment of an administrator or receiver (including as administrative receiver or manager), conciliator, trustee, assignee, custodian, sequestrator, liquidator or similar official under any bankruptcy law, of such Financial Guarantor (or as the case may be, of a material part of its property or assets) under any Bankruptcy Law;
  - (ii) makes or enters into any general assignment, composition, arrangement (including a voluntary arrangement under the Insolvency Act 1986) or compromise with or for the benefit of any of its creditors;
  - (iii) has a final and non-appealable order for relief entered against it under any Bankruptcy Law; or
  - (iv) has a final and non-appealable order, judgment or decree of a court of competent jurisdiction entered against it appointing any conciliator, receiver, administrative receiver, trustee, assignee, custodian, sequestrator, liquidator, administrator or similar official under any Bankruptcy Law (each a “**Custodian**”) for such Financial Guarantor or all or any material portion of its property or authorising the taking of its possession by a Custodian of such Financial Guarantor;

For the purpose of this definition, “**Bankruptcy Law**” means Law No. 85-98 of 25 January 1985 and Law No 84-148 of 1 March 1984 of the French Republic, any similar or future federal or state bankruptcy, insolvency, reorganisation, moratorium, rehabilitation, fraudulent conveyance or similar law, statute or regulation of the French Republic or of any other applicable jurisdiction for the relief of debtors, and, in relation to any other Financial Guarantor, such events as are specified in that Financial Guarantor’s I&I Agreement or equivalent document and set out in the relevant Final Terms;

**“Final Determination”**

means the final price determination made by the DGWS on a five-yearly basis;

**“Final Terms”**

means the final terms issued in relation to each Tranche of Bonds and giving details of that Tranche;

**“Finance Documents”**

the Security Documents, Bond Trust Deed and the Existing Bond Trust Deeds, the Bonds (including the applicable Final Terms), the Bond Policies, the I&I Agreements, the Premium Letters, the Finance Lease Documents, the Hedging

Agreements, the CTA, the Issuer/Anglian Water Loan Agreement, the Anglian Water Loan Notes, the Initial Authorised Loan Agreement, the Bridging Facility Agreement, the Liquidity Facility Agreements, the Agency Agreement, the Existing Agency Agreements, the Master Definitions Agreements, the Account Bank Agreement, the CP Document, the Note Purchase Agreement, any other Authorised Credit Facilities, the Indemnification Deed, the Tax Deed of Covenant, the Programme Agreement and each agreement or other instrument between Anglian Water or the Issuer (as applicable) and an additional Secured Creditor designated as a Finance Document by Anglian Water or the Issuer (as applicable) and such additional Secured Creditor in the Accession Memorandum for such additional Secured Creditor;

**“Finance Lease Documents”**

means each Finance Lease together with any related or ancillary documentation;

**“Finance Leases”**

means the Existing Finance Leases and any new finance lease entered into by Anglian Water or the Issuer in respect of plant, machinery, software, computer systems or equipment (the counterparty to which has acceded to the terms of the STID and the CTA and has agreed to be bound by the terms of Part 2 of Schedule 14 (Finance Lease Terms) of the CTA) permitted to be entered into under the terms of the CTA, each a **“Finance Lease”**;

**“Finance Lessors”**

means the Existing Finance Lessors, Barclays Technology Finance Limited and any other person entering into a Finance Lease with Anglian Water, as permitted by the CTA and the STID, who accedes to the STID and the CTA as a Finance Lessor (each a **“Finance Lessor”**);

**“Finance Party”**

means any person providing financial accommodation pursuant to an Authorised Credit Facility including all arrangers, agents and trustees appointed in connection with any such Authorised Credit Facilities;

**“Financial Guarantor”**

means any person, including the Initial Financial Guarantor, which provides a financial guarantee insurance policy, including the Bond Policies, in respect of any of the Wrapped Debt, and **“Financial Guarantors”** means all of them if there is more than one at any time;

**“Financial Indebtedness”**

means any indebtedness for or in respect of:

- (a) monies borrowed or raised (whether or not for cash);
- (b) any documentary or standby letter of credit facility;
- (c) any acceptance credit;
- (d) any bond, note, debenture, loan stock or other similar instrument;
- (e) any finance, capital lease or hire purchase contract which would, in accordance with Applicable Accounting Principles, be treated as such;
- (f) any amount raised pursuant to any issue of shares which are capable of redemption;

- (g) receivables sold or discounted (otherwise than on a non-recourse basis);
- (h) the amount of any liability in respect of any advance or deferred purchase agreement if either one of the primary reasons for entering into such agreement is to raise finance or the relevant payment is advanced or deferred for a period in excess of 90 days;
- (i) any termination amount due from any member of the Anglian Water Services Financing Group in respect of any Treasury Transaction that has terminated;
- (j) any other transaction (including any forward sale or purchase agreement) which has the commercial effect of a borrowing;
- (k) any counter-indemnity obligation in respect of any guarantee, indemnity, bond, letter of credit or any other instrument issued by a bank or financial institution; or
- (l) any guarantee, indemnity or similar assurance against financial loss of any person in respect of any item referred to in paragraphs (a) to (k) above;

**“Financial Year”**

means the twelve months ending on the 31 March in each year or such other period as may be approved by the Security Trustee;

**“Fitch”**

means Fitch Ratings Limited;

**“Global Bond”**

means a Temporary Bearer Global Bond and/or a Permanent Bearer Global Bond and/or a Regulation S Global Bond and/or a Rule 144A Global Bond, as the context may require;

**“Good Industry Practice”**

means the standards, practices, methods and procedures as practised in the United Kingdom conforming to all applicable laws and that degree of skill, diligence, prudence and foresight which would reasonably be expected from a skilled and experienced person undertaking all or part of the Business as the case may be, under the same or similar circumstances having regard to the regulatory pricing allowances and practices in the United Kingdom’s regulated water and sewerage industry at the relevant time;

**“Habitats Regulations”**

means the Conservation (Natural Habitats etc.) Regulations 1994 implemented pursuant to Council Directive 92/43/EEC;

**“Hedge Counterparty”**

means any counterparty to a Hedging Agreement which is or becomes a party to the STID in accordance with the STID, including the Existing Hedge Counterparties, BNP Paribas, Morgan Stanley & Co. International Limited and SMBC Capital Markets, Inc. and **“Hedge Counterparties”** means any or all parties as the context requires;

**“Hedging Agreement”**

means:

- (a) the Existing Hedging Agreements;
- (b) any Treasury Transaction entered or to be entered into by the Issuer with Hedge Counterparties in accordance with the Hedging Policy (the counterparties to which have acceded to the terms of the STID and the CTA

and agreed to be bound by the terms of Schedule 8 (Hedging Policy and Overriding Provisions relating to Hedging Agreements) of the CTA); and

- (c) any other Treasury Transaction (the counterparties to which have acceded to the terms of the STID and the CTA and agreed to be bound by the terms of Schedule 8 (Hedging Policy and Overriding Provisions relating to Hedging Agreements) of the CTA) designated a Hedging Agreement by the Security Trustee and the Issuer;

<b>“Hedging Policy”</b>	means the initial hedging policy applicable to Anglian Water and the Issuer set out in Schedule 8 (Hedging Policy and Overriding Provisions relating to Hedging Agreements) of the CTA as such hedging policy may be amended from time to time by agreement between the Security Trustee and the Issuer in accordance with the STID;
<b>“Holding Company”</b>	means a holding company within the meaning of section 736 of the Companies Act 1985;
<b>“I&amp;I Agreement”</b>	means each insurance and indemnity agreement (or similarly named agreement) between, <i>inter alios</i> , the Issuer and a Financial Guarantor in connection with a particular Series of Class A Wrapped Bonds and/or Class B Wrapped Bonds;
<b>“IDOK”</b>	means an interim determination of K as provided for in Part IV of Condition B of the Instrument of Appointment;
<b>“Indemnification Deed”</b>	means the deed so named and dated on or about the Effective Date between the Obligors, any Financial Guarantor and the Dealers;
<b>“Independent Review”</b>	means an independent review resulting from a Trigger Event as defined in Section 7.5.8 (iii), “ <i>Financing Structure – Common Terms Agreement – Trigger Event Consequences – Independent Review</i> ”;
<b>“Initial Authorised Credit Providers”</b>	means any party to the Initial Authorised Loan Agreement as lender or Finance Party;
<b>“Initial Authorised Loan Agreement”</b>	means the bank facility entered into between, <i>inter alios</i> , the Issuer and the Initial Authorised Credit Providers on or about the Effective Date;
<b>“Initial Authorised Credit Facility Agent”</b>	means Barclays Bank PLC or any successor thereto;
<b>“Initial Authorised Credit Facility Arranger”</b>	means Barclays Capital, or any successor thereto;
<b>“Initial Bond Policies”</b>	means the financial guarantee policies issued by the Initial Financial Guarantor (subject to the satisfaction of certain conditions) in connection with the first Series of Wrapped Bonds;
<b>“Initial Financial Guarantor”</b>	means MBIA Assurance S.A.;
<b>“Initial Liquidity Facility Provider”</b>	means Barclays Bank PLC;
<b>“Insolvency Act”</b>	means the Insolvency Act 1986;
<b>“Insolvency Act 2000”</b>	means the Insolvency Act 2000, certain provisions of which were brought into force on 1 January 2003;

**“Insolvency Event”**

means, in respect of any company:

- (a) the initiation of or consent of Insolvency Proceedings by such company or any other company or the presentation of a petition for the making of an administration order and, in the opinion of the Security Trustee, such proceedings not being disputed in good faith with a reasonable prospect of success;
- (b) the making of an administration order in relation to such company;
- (c) an encumbrancer (excluding in relation to the Issuer, the Bond Trustee or any receiver) taking possession of the whole or any part of the undertaking or assets of such company;
- (d) any distress, execution, attachment or other process being levied or enforced or imposed upon or against the whole or any part of the undertaking or assets of such person (excluding in relation to the Issuer, the Security Trustee or any receiver) and such order, appointment, possession or process (as the case may be) not being discharged or otherwise ceasing to apply within 30 days;
- (e) the making of an arrangement, composition, reorganisation with or conveyance to or assignment for the creditors of such company generally or the making of an application to a court of competent jurisdiction for protection from the creditors of such company generally;
- (f) a meeting is convened for the purpose of considering a resolution or an effective resolution is passed or an order is made by a court of competent jurisdiction for the winding-up or dissolution of such company (except, in the case of the Issuer, a winding-up for the purpose of a merger, reorganisation or amalgamation the terms of which have previously been approved either in writing by the Security Trustee or by an Extraordinary Resolution);
- (g) the appointment of an Insolvency Official in relation to such company or in relation to the whole or any substantial part of the undertaking or assets of such company;
- (h) save as permitted in the STID, the cessation or suspension of payment of its debts generally or a public announcement by such person of an intention to do so; or
- (i) save as provided in the STID, a moratorium is declared in respect of any indebtedness of such person;

**“Insolvency Official”**

means, in respect of any company, a liquidator, provisional liquidator, administrator, Special Administrator, administrative receiver, receiver or manager, nominee, supervisor, trustee, conservator, guardian or other similar official in respect of such company or in respect of all or

substantially all of the company's assets or in respect of any arrangement or composition with creditors;

**“Insolvency Proceedings”**

means the winding-up, dissolution, administration or special administration of a company, corporation or other person or any equivalent or analogous proceedings under the law of the jurisdiction in which such company or corporation is incorporated or of any jurisdiction in which such company or corporation carries on business, including the seeking of liquidation, winding-up, reorganisation, dissolution, administration, special administration, arrangement, adjustment, protection or relief of debtors;

**“Institutional Accredited Investor”**

means an institutional investor that qualifies as an “accredited investor” (as defined in Rule 501(a)(1), (2), (3) or (7) under the Securities Act) and that is not a QIB;

**“Instructing Group”**

means the Class A DIG or, following repayment in full of the Class A Debt, the Class B DIG;

**“Instrument of Appointment” or “Licence”**

means the instrument of appointment dated August 1989 under sections 11 and 14 of the Water Act 1989 (as in effect on 1 August 1989) under which the Secretary of State for the Environment appointed Anglian Water as a water and sewerage undertaker under that Act for the areas described in the Instrument of Appointment as modified or amended from time to time;

**“Intercompany Loan”**

means the principal amount of all advances from time to time outstanding under the Intercompany Loan Arrangements;

**“Intercompany Loan Arrangements”**

means the Issuer/Anglian Water Loan Agreement and/or the Anglian Water Loan Notes, as the context requires;

**“Intercreditor Arrangements”**

means the arrangements between the Secured Creditors of the Anglian Water Services Financing Group in the STID summarised in Section 7.3, “*Financing Structure – Security Trust and Intercreditor Deed*”;

**“Interest Payment Date”**

means any date upon which interest or payment equivalent to interest become payable under the terms of any Authorised Credit Facility;

**“Interest Rate Hedging Agreement”**

means a Treasury Transaction to swap interest rates;

**“Investment Company Act”**

means the U.S. Investment Company Act of 1940, as amended, and the rules and regulations promulgated thereunder;

**“Investment Grade”**

means a rating of at least BBB – by Fitch, Baa3 by Moody ‘s or BBB – by S&P;

**“Investors Report”**

means each report produced by Anglian Water and the Issuer within the earlier of 45 days after publication of the relevant Financial Statements or 180 days from 31 March or 90 days from 30 September in each year in respect of the immediately preceding calendar half year starting with 30 September 2002, in substantially the form set out in the CTA provided that ratio calculations will be adjusted only for every second Investors' Report;

**“IP”**

means intellectual property;

<b>“IPPC”</b>	means the integrated pollution prevention and control regime introduced by the United Kingdom Pollution Prevention and Control Act 1999;
<b>“IRC”</b>	means the amounts set out under the heading infrastructure renewals charge in the financial projections contained in the supplementary report issued by Ofwat detailing the numbers and assumptions specific to Anglian Water in the DGWS’s most recent Final Determination adjusted as appropriate for any subsequent IDOK and for Out-turn Inflation;
<b>“Issue Date”</b>	means the date of issue of any Series of Bonds or the date upon which all conditions precedent to any other Authorised Credit Facility have been fulfilled or waived and the Issuer makes a utilisation of that facility;
<b>“Issuer”</b>	means Anglian Water Services Financing Plc;
<b>“Issuer/Anglian Water Loan Agreement” and “Issuer/AWS Loan Agreement”</b>	means the loan agreement entered into between the Issuer and Anglian Water on 30 July 2002 as more particularly defined in Section 7.4.2, “ <i>Financing Structure – Intercompany Loan Arrangements – Issuer/Anglian Water Loan Arrangements</i> ”;
<b>“IT”</b>	means information technology;
<b>“K”</b>	means the adjustment factor set for each year by the DGWS by which charges made by Regulated Companies for water supply and sewerage services may be increased, decreased or kept constant;
<b>“Lease Calculation Cashflow”</b>	means, in respect of any Test Period or, as the case may be, the Pre-Test Period, for any Finance Lease, a cashflow statement produced by the relevant Finance Lessor on, or as soon as reasonably practicable after, its Lease Calculation Date occurring prior to the commencement of such Test Period and in accordance with its terms and Schedule 14 ( <i>Finance Lease Terms</i> ) of the CTA and, in the case of an Additional Secured Creditor, in accordance with the terms of the relevant Accession Memorandum and using, inter alia, for the purposes of calculating the amount shown for each rental payment date falling within the Test Period or, as the case may be, the Pre-Test Period under the heading “interest” (or the equivalent thereof (howsoever worded)) in such cashflow statement, a rate of LIBOR, estimated, as at its Lease Calculation Date, by reference to the average of those rates per annum being offered by the reference banks specified in the relevant finance lease (or where there is none, Barclays Bank PLC and Citibank N.A.) to prime banks in the London interbank market for entry into 12 month (or such other period as is equal to the relevant rental period under such Finance Lease) forward contracts, commencing on each rental payment date arising during the period commencing on such Lease Calculation Date and ending on the last rental payment date to occur during the relevant Test Period and as agreed between Anglian Water and the relevant Finance Lessor (provided that, where any Finance Lease contains Rentals which are calculated by reference to a fixed rate of interest, any Lease Calculation Cashflow produced in respect of that Finance Lease shall reflect the actual fixed rate of interest implicit in such Rental calculations), provided that where in respect of any Finance Lease there has been a change of assumption resulting in an

increase or decrease in the Rental payable thereunder during any Test Period or the Pre-Test Period, as the case may be, the Lease Calculation Cashflow applicable to that Finance Lease for such Test Period or the Pre-Test Period shall also include a cashflow statement, produced as soon as reasonably practicable after the time of recalculating the Rental in accordance with the terms of that Finance Lease and Schedule 14 (Finance Lease Terms) of the CTA or, as the case may be, that Accession Memorandum and using, in such cashflow statement, the same estimated interest rates as were used in preparation of the original cashflow statement prepared on or as soon as reasonably practicable after the Lease Calculation Date applicable to that Test Period or the Pre-Test Period, as the case may be;

**“Lease Calculation Date”**

means in respect of any Existing Finance Lease:

- (a) the Effective Date; and
- (b) the date falling 10 days before the rental payment date immediately preceding 1 April 2003; and
- (c) each yearly anniversary of the date referred to in (b) above,

and in respect of any Finance Lease which is not an Existing Finance Lease:

- (x) the date of the Accession Memorandum executed by the relevant Finance Lessor relating to such Finance Lease; and
- (y) the date falling 10 days before the rental payment date immediately preceding the commencement date of the first Test Period to commence immediately after the date referred to in (x) above; and
- (z) each yearly anniversary of the date referred to in (y) above,

save that where any date referred to in (b), (c), (x), (y) or (z) is not a Business Day, such date shall be deemed to be the preceding Business Day.

**“Lease Reserve Amount”**

means in respect of any Finance Lease in any Test Period, the lower of (i) the aggregate Notional Amount calculated with respect to such Finance Lease; and (ii) the aggregate amount of rental payments payable to the Finance Lessor under such Finance Lease in respect of such Test Period or, as the case may be, the Pre-Test Period (inclusive of value added tax) (after adding back any additional rentals (inclusive of value added tax) payable and deducting any estimated rental rebates (inclusive of any credit for value added tax), in each case as determined in accordance with the provisions of the relevant Finance Lease);

**“Licence” or “Instrument of Appointment”**

means the instrument of appointment dated August 1989 under Sections 11 and 14 of the Water Act 1989 (as in effect on 1 August 1989) under which the Secretary of State for the Environment appointed Anglian Water as a water and sewerage undertaker under the Act for the areas described in



	the Instrument of Appointment, as modified or amended from time to time;
<b>“Liquidity Facility”</b>	means a Debt Service Reserve Liquidity Facility or an O&M Reserve Facility made available under a Liquidity Facility Agreement and <b>“Liquidity Facilities”</b> means all of them;
<b>“Liquidity Facility Agent”</b>	means in respect of the Debt Service Reserve Liquidity Facility Agreements and the O&M Reserve Facility Agreement, Barclays Bank PLC;
<b>“Liquidity Facility Agreements”</b>	means the Debt Service Reserve Liquidity Facility Agreements and the O&M Reserve Facility Agreement;
<b>“Liquidity Facility Provider”</b>	means any lender from time to time under a Liquidity Facility Agreement, including, the Debt Service Reserve Liquidity Facility Provider and the O&M Reserve Facility Provider;
<b>“Liquidity Facility Requisite Ratings”</b>	means the Minimum Short-term Rating and a minimum long-term rating of at least “A” from Fitch and S&P and at least “A2” from Moody’s from at least two Rating Agencies;
<b>“Local Authority Loan”</b>	means the local authority loan in the amount of approximately £172,000 provided to Anglian Water by Castle Point Borough Council;
<b>“London Stock Exchange”</b>	means the London Stock Exchange plc;
<b>“Majority Creditors”</b>	means Class A DIG Representatives in respect of more than 50 per cent. of the Voted Qualifying Class A Debt or following the repayment in full of the Class A Debt, Class B DIG Representatives in respect of more than 50 per cent. of the Voted Qualifying Class B Debt, in each case subject to Clause 8 (Modifications, Consents and Waivers) and Clause 9 (Voting Instructions and Notification of Outstanding Principal Amounts of Qualifying Debt) of the STID;
<b>“Make-Whole Amount”</b>	means the Make-Whole Amount as defined in the Conditions and/or the Note Purchase Agreement relating to the USPP 2001 Bonds and any other amount above par payable on redemption of any Class A Debt or Class B Debt except where such amount is limited to accrued interest;
<b>“Master Definitions Agreement”</b>	means the Master Definitions Agreement dated 30 July 2002 between the Obligors and the other parties named therein as amended by an amending agreement to the Master Definitions Agreement dated on or about 23 September 2005;
<b>“Material Adverse Effect”</b>	means the effect of any event or circumstance which is materially adverse, taking into account the timing and availability of any rights or remedies under the WIA or the Instrument of Appointment, to: <ul style="list-style-type: none"> <li>(a) the business, property, operations or financial condition of Anglian Water or of the Anglian Water Services Financing Group as a whole;</li> <li>(b) the ability of any member of the Anglian Water Services Financing Group to perform its obligations under any Finance Document;</li> </ul>

	(c) the validity or enforceability of any Finance Document or the rights or remedies of any Secured Creditor thereunder; or
	(d) the ability of Anglian Water to perform or comply with any of its obligations under the Instrument of Appointment or the WIA;
<b>“Material Agreement”</b>	means any Tier 1 Material Agreement or Tier 2 Material Agreement;
<b>“Material Entity Event”</b>	means any of the events or circumstances in Schedule 2 to the CTA and described in Section 7.5.11, “ <i>Financing Structure – Common Terms Agreement – Material Entity Events</i> ”;
<b>“Maturity Date”</b>	means the date on which a Bond is expressed to be redeemable or any other Authorised Credit Facility is expressed to be repayable in full;
<b>“Maximum Early Redemption Amount”</b>	means the aggregate of all Early Redemption Amounts which would become payable upon redemption of USPP 2001 Bonds following the occurrence of an Early Redemption Event, assuming the holders of all USPP 2001 Bonds which were entitled to do so elected to have their USPP 2001 Bonds redeemed as a result of an Early Redemption Event occurring;
<b>“MBIA”</b>	means MBIA Assurance S.A.;
<b>“MBIA Make-Whole Amount”</b>	means the amount of market value in excess of par paid out by MBIA in respect of £100,000,000 5½ per cent. index-linked loan stock due 2008 and £100,000,000 12 per cent. bonds due 2014, as further defined in the Bond Policy relating to such bonds;
<b>“Meter Optants”</b>	means domestic customers who have opted to be charged on the basis of a meter reading rather than by rateable value;
<b>“Minimum Long-term Rating”</b>	means, in respect of any person, such person’s long-term unsecured debt obligations being rated, in the case of Moody’s, “Aa3”; in the case of S&P, “AA-”; and in the case of Fitch, “AA-”
<b>“Minimum Short-term Rating”</b>	means, in respect of any person, such person’s short-term unsecured debt obligations being rated, in the case of Moody’s, “Prime-1”; and in the case of S&P, “A-1”; and in the case of Fitch, “F-1”;
<b>“MI/d”</b>	means megalitres per day;
<b>“Monthly Payment Amount”</b>	means the amount paid on a monthly basis by Anglian Water to the Debt Service Payment Account, as defined in Section 7.6.3, “ <i>Financing Structure – Cash Management – Payment Account</i> ”;
<b>“Moody’s”</b>	means Moody’s Investors Service Limited;
<b>“Net Cash Flow”</b>	means: <ul style="list-style-type: none"> <li>(a) in respect of any historical element of a Test Period, the aggregate of net cash flow from operating activities as shown in the Anglian Water financial statements, (after adding back, without double counting, and to the extent that such items are included in net cash flow</li> </ul>

from operating activities, any exceptional items, any customer rebates, any recoverable VAT, any capital maintenance expenditure and any movement in debtors and/or creditors relating to capital expenditure) minus corporation tax paid; and

- (b) in respect of any forward looking element of a Test Period shall have the same meaning set out in (a) above save that that paragraph shall be amended by adding the words “less any net cash flow from operating activities of its business other than its Regulated Business and after adding back corporation tax paid arising as a result of such businesses” after the words “corporation tax paid”;

**“New Money Advance”**

means any drawing during a Standstill under a Liquidity Facility or any Authorised Credit Facility which is not made (or to the extent not made) for the purpose of refinancing a maturing Advance under such Liquidity Facility or refinancing a drawing under such Authorised Credit Facility;

**“Non-Regulatory Allowable Expense”**

means any expense incurred in connection with activities that are not the subject of, or fall outside the scope of, any Periodic Review;

**“Note Purchase Agreement”**

means the note purchase agreement dated 25 July 2001 pursuant to which Anglian Water issued the USPP 2001 Bonds;

**“Notified Item”**

means any item formally notified by the DGWS to the Regulated Company as not having been allowed for in K, provided that there has been no Periodic Review subsequent to that notification;

**“Notional Amount”**

means, in respect of any Finance Lease, a sum, certified by any duly authorised signatory of the relevant Finance Lessor on each Lease Calculation Date and using the relevant Lease Calculation Cashflow relating thereto as being, for the succeeding Test Period, the amount shown for each rental payment date falling in that relevant Test Period or, as the case may be, the Pre-Test Period under the headings “interest” and “margin” (or any equivalents thereof (howsoever worded)) in the relevant Lease Calculation Cashflow, together with an amount equal to VAT on such amount at the rate applicable to rentals payable under the relevant Finance Lease;

**“NPV”**

means, in respect of any amount payable or receivable at a future date, such amount discounted back to the date of calculation on an annual basis at the long term weighted average cost of funds of Anglian Water calculated on the basis of all Financial Indebtedness of Anglian Water having a residual maturity in excess of 12 months and the applicable rates of interest thereon;

**“O&M Reserve Account”**

means the account of Anglian Water entitled “O&M Reserve Account” held at the Account Bank and includes any sub-account relating to that account and any replacement account from time to time;

**“O&M Reserve Facility”**

means an operation and maintenance reserve liquidity facility made available under a Liquidity Facility Agreement;

<b>“O&amp;M Reserve Facility Agreement”</b>	means an agreement establishing an O&M Reserve Facility as more particularly described in Section 7.9.4, “ <i>Financing Structure – Additional Resources Available – The Liquidity Facilities</i> ”;
<b>“O&amp;M Reserve Facility Provider”</b>	means the provider of the O&M Reserve Facility from time to time;
<b>“Obligor”</b>	means any member of the Anglian Water Services Financing Group and “ <b>Obligors</b> ” means all of them;
<b>“Official List”</b>	means the official list of the United Kingdom Listing Authority;
<b>“OFT”</b>	means the Office of Fair Trading in the United Kingdom;
<b>“Ofwat”</b>	means the Office of Water Services in England and Wales;
<b>“Operational Performance Assessment”</b>	means the assessment performed by Ofwat to monitor water company performance;
<b>“Ordinary Distribution”</b>	means a Distribution which is paid out of Net Cash Flow generated, but taking account of interim dividends, during the twelve months up to 31 March (being the final dividend for that Financial Year) or Net Cash Flow generated during the six months up to 30 September (being the interim dividend for the first half of that Financial Year);
<b>“Original Lender”</b>	means a lender under the Bridging Facility;
<b>“Outsourcing Agreement”</b>	means any agreement pursuant to which Anglian Water sub-contracts, tenders or outsources either the day-to-day operation of its assets and service delivery (including any maintenance expenditure) that Anglian Water could, if not outsourced, perform itself and which has (or would have were it entered into on arm’s length terms) an annual value in excess of £100,000 (indexed);
<b>“Outsourcing Policy”</b>	means each of the obligations in Schedule 9 (Outsourcing Policy) of the CTA;
<b>“Outstanding Principal Amount”</b>	means, as at any date that the same falls to be determined: <ul style="list-style-type: none"> <li>(a) in respect of Wrapped Bonds prior to the occurrence of an FG Event of Default which is continuing, the aggregate of any unpaid amounts owing to a Financial Guarantor under an I&amp;I Agreement to reimburse it for any amount paid by it under a Bond Policy in respect of unpaid principal on a Wrapped Bond and the principal amount outstanding (or the Equivalent Amount) of the Wrapped Bonds (including any premium);</li> <li>(b) in respect of Wrapped Bonds after an FG Event of Default which is continuing, the principal amount outstanding (or the Equivalent Amount) of the Wrapped Bonds (including any premium);</li> <li>(c) in respect of Unwrapped Bonds, the principal amount outstanding (or the Equivalent Amount) of the Unwrapped Bonds (including any premium);</li> </ul>

- (d) in respect of any Authorised Credit Facilities that are loans, the principal amount (or the Equivalent Amount) of any drawn amounts that are outstanding;
- (e) in respect of each Finance Lease, the Equivalent Amount of either (i) prior to an Acceleration of Liabilities (other than a Permitted Lease Termination) and subject to any increase or reduction calculated in accordance with Clause 9.9 (Notification of Outstanding Principal Amount of Qualifying Debt) of the STID, the highest termination value which may fall due during the rental period encompassing such date, calculated upon the assumptions set out in the cashflow report provided by the relevant Finance Lessor on the first day of each such rental period (or in the most recently generated cash flow report which is current on such date) or (ii) following any Acceleration of Liabilities (other than a Permitted Lease Termination), the actual amount (if any) that would be payable to the relevant Finance Lessor in respect of a termination of the leasing of the Equipment on the date of such Acceleration of Liabilities (other than a Permitted Lease Termination);
- (f) in respect of any other Secured Liabilities, the Equivalent Amount of the outstanding principal amount of such debt on such date in accordance with the relevant Finance Document;

all as most recently certified or notified to the Security Trustee, where applicable, pursuant to Clause 9.9 (Notification of Outstanding Principal Amount of Qualifying Debt) of the STID;

**“Out-turn Inflation”**

means, in respect of any period for which the relevant indices have been published, the actual inflation rate applicable to such period determined by reference to movements in the RPI adjusted, as appropriate, in the case of capital additions, for any divergence between the actual movement of national construction costs, as evidenced by the Construction Output Price Index (or such other index as the DGWS may specify) relative to the RPI from their base levels as used in the most recent Final Determination or IDOK and their relative movement as projected by the DGWS for the purposes of that determination, and in respect of any period, including future periods, for which the relevant indices have not yet been published, by reference to forecast rates consistent with the average monthly movement in such indices over the previous 12 months for which published indices are available;

**“Participating Member State”**

means a member state of the European Community that adopts or has adopted the euro as its lawful currency under the legislation of the European Union for European Monetary Union;

**“Paying Agents”**

means, in relation to all or any Series of the Bonds, the several institutions (including, where the context permits, the Principal Paying Agent) at their respective specified offices initially appointed as paying agents in relation to such Bonds by the Issuer and the Obligors pursuant to the Agency Agreement and/or, if applicable, any successor paying agents

at their respective specified offices in relation to all or any Series of the Bonds;

**“Payment Account”**

means the account of Anglian Water titled “Payment Account” held at the Account Bank and includes any sub-account relating to that account and any replacement account from time to time;

**“Payment Date”**

means each date on which a payment is made or is scheduled to be made by any Obligor in respect of any obligations or liabilities under any Authorised Credit Facility;

**“Payment Priorities”**

means the provisions relating to the order of priority of payments set out in Section 7.6.5, “*Financing Structure – Cash Management – Debt Service Payment Account*”;

**“Periodic Review”**

means the periodic review of K (as that term is defined in the Instrument of Appointment) as provided for in Part III of Condition B of the Instrument of Appointment;

**“Period Review Effective Date”**

means the date with effect from which the new K (as that term is defined in the Instrument of Appointment) will take effect, following a Periodic Review;

**“Permanent Bearer Global Bond”**

means a global bond comprising some or all of the Bearer Bonds of the same Series issued by the Issuer in exchange for the whole or part of any Temporary Bearer Global Bond issued in respect of such Bearer Bonds;

**“Permitted Acceleration”**

means an acceleration of certain share pledges permitted pursuant to the STID;

**“Permitted Acquisition”**

means any of the following carried out by Anglian Water:

- (a) acquisitions (including Authorised Investments) made on arm’s length terms and in the ordinary course of trade;
- (b) acquisitions of assets required to replace surplus, obsolete, worn-out, damaged or destroyed assets which in the reasonable opinion of Anglian Water are required for the efficient operation of its Business or in accordance with the Finance Leases; or
- (c) acquisition of assets (but not companies or joint ventures) made on arm’s length terms entered into for *bona fide* commercial purposes in furtherance of Anglian Water’s statutory and regulatory obligations;

but not an acquisition of a water business or interest therein (except (i) for inset business in the United Kingdom which is or will be included in RAV and which breaches neither the Instrument of Appointment nor the Act or (ii) with the prior consent of the Security Trustee and each Financial Guarantor);

**“Permitted Book Debt Disposal”**

means the disposal (with the prior consent of the Security Trustee and each Financial Guarantor) of book debts by Anglian Water on arm’s length terms to any person other than an Affiliate, provided that where such book debts are sold on recourse terms:

- (a) Anglian Water has made a prudent provision in its accounts against the non-recoverability of such debts;

- (b) the recourse period does not exceed 24 months;
- (c) any write-back of any provision for non-recoverability arising from the sale can only be treated as operating profit for the purposes of the financial ratios once the relevant recourse period against Anglian Water has expired; and
- (d) the Anglian Water Business Financial Model is updated to ensure the transaction is taken into account in calculating all relevant financial ratios under the CTA;

**“Permitted Demerger”**

means a demerger, reconstruction, scheme of arrangement or other like process immediately following which either (i) no person Controls Anglian Water Services Holdings Ltd or (ii) all of Anglian Water Services Holdings Ltd’s shares (or the shares of any company of which Anglian Water Services Holdings Ltd is a direct or indirect wholly-owned subsidiary) are held by the then existing shareholders of AWG;

**“Permitted Disposal”**

means any disposal made by Anglian Water which:

- (a) is made in the ordinary course of trading of the disposing entity or in connection with an arm’s length transaction entered into for *bona fide* commercial purposes for the benefit of the Business;
- (b) is of assets in exchange for other assets comparable or superior as to type, value and quality;
- (c) is of Equipment pursuant to the Finance Leases;
- (d) would not result in the Senior RAR, calculated for each Test Period by reference to the most recently occurring Calculation Date (adjusted on a pro-forma basis to take into account the proposed disposal) being less than or equal to 0.9:1;
- (e) is a disposal for cash on arm’s length terms of any surplus or obsolete or worn-out assets which, in the reasonable opinion of Anglian Water, are not required for the efficient operation of its Business and which does not cause a Trigger Event under paragraph 1 of Schedule 6, Part 1 of the CTA;
- (f) is a Permitted Book Debt Disposal;
- (g) is a disposal of Protected Land (as that term is defined in the Act) in accordance with the terms of the Instrument of Appointment;
- (h) is a disposal or surrender of tax losses which is a Permitted Tax Loss Transaction; or
- (i) is any other disposal which is in accordance with the Instrument of Appointment provided that the consideration (both cash and non-cash) received by Anglian Water (or which would be received by Anglian Water if such disposal was made on arm’s length terms for full commercial value to an unconnected third party) in respect of any such

disposal when aggregated with all other such disposals by it made in (y) the immediately preceding 12 month period does not exceed 2½ per cent. of RAV (or its equivalent) and (z) in the immediately preceding five-year period does not exceed 10 per cent. of RAV (or its equivalent);

provided that in each case such disposal does not cause the Trigger Event Ratio Levels to be breached;

**“Permitted Emergency Action”**

means any remedial action taken by Anglian Water during an Emergency which is in accordance with the policies, standards and procedures for emergency planning manual (EMPROC) of Anglian Water (as amended from time to time), Ofwat guidance notes and Public Procurement Rules and which Anglian Water considers necessary and which continues only so long as required to remedy the Emergency but in any event no longer than 28 days or such longer period as is agreed by Anglian Water, the Security Trustee and each Financial Guarantor;

**“Permitted Existing Non-Statutory Business”**

means any business other than the Regulated Business which is carried on by Anglian Water at the Effective Date and (a) which falls within the Permitted Non-Statutory Business Limits applicable to Permitted Existing Non-Statutory Business and (b) in respect of which all material risks related thereto are fully insured and (c) which does not give rise to any material, actual or contingent liabilities for Anglian Water that are not properly provided for in its financial statements;

**“Permitted Financial Indebtedness”**

means:

- (a) Financial Indebtedness incurred under the Intercompany Loan Arrangements or the UK Holdco/Anglian Water Loan;
- (b) Financial Indebtedness incurred under any Finance Document as at the Effective Date;
- (c) Financial Indebtedness incurred under a Treasury Transaction provided it is in compliance with the Hedging Policy;
- (d) the Local Authority Loan provided that the aggregate amount thereof does not exceed the amount at the date of the CTA;
- (e) any unsecured indebtedness which is fully subordinated to the Class A Debt and Class B Debt in a manner satisfactory to the Security Trustee provided that the aggregate amount of such Financial Indebtedness, when aggregated further with those amounts outstanding under the facilities referred to in paragraph (d) above does not exceed £15,000,000 (indexed);
- (f) any Subordinated Debt;
- (g) such further Financial Indebtedness incurred by the Issuer or Anglian Water that complies with the following conditions:



- (i) at the time of incurrence of that Financial Indebtedness, no Default is continuing or will arise as a result of the incurrence of such Financial Indebtedness;
- (ii) the Financial Indebtedness is made available pursuant to an Authorised Facility Agreement the counterparty to which has acceded to the CTA and STID;
- (iii) as a result of the incurrence of the Financial Indebtedness:
  - (A) Anglian Water and the Issuer will not be in breach of its covenant to maintain the Debt Service Reserve Liquidity Facility to the required level as more particularly described in Section 7.5.6(ii)(a), "*Financing Structure – Common Terms Agreement – Covenants – Financial Covenants*" and its covenant to ensure scheduled final repayments are controlled, as more particularly described in Section 7.5.5(vii)(e), "*Financing Structure – Common Terms Agreement – Covenants – Covenants General*";
  - (B) no Authorised Credit Provider will have better or additional Entrenched Rights under the STID than those Authorised Credit Providers of the same class; and
  - (C) the Hedging Policy shall continue to be complied with in all respects;
- (iv) the Financial Indebtedness which is Class A Debt ranks pari passu in all respects with all other Class A Debt and the Financial Indebtedness that is Class B Debt ranks pari passu in all respects with all other Class B Debt;
- (v) if such further Financial Indebtedness is Class A Debt or Class B Debt then the Senior RAR (adjusted on a proforma basis to take into account the proposed incurrence of such further Financial Indebtedness) must be less than or equal to 0.90: 1 for each Test Period calculated by reference to the then most recently occurring Calculation Date;
- (vi) if such further Financial Indebtedness is Class A Debt then (taking into account the incurrence of such debt) the Class A RAR must be less than or equal to 0.75:1 and the Class A PMICR must be greater than or equal to 1.30:1 for each Test Period calculated by reference to the then most recently occurring Calculation Date;

- (vii) if such further Financial Indebtedness is incurred under a Finance Lease, the amount of that Financial Indebtedness, when aggregated with all other Financial Indebtedness under Finance Leases shall not exceed an amount of £570,000,000 (indexed);
- (h) Financial Indebtedness incurred with the consent of the Security Trustee and each Financial Guarantor.

For the purposes of this definition only, the termination sums payable under a Treasury Transaction that has been terminated shall not be treated as Financial Indebtedness and the occurrence of such event shall not be construed as the inurrence of Financial Indebtedness;

**“Permitted Hedge Termination”**

means the termination of a Hedging Agreement in accordance with the CTA;

**“Permitted Joint Venture”**

means, after the Effective Date, the financing, development, design, carrying out and management by or on behalf of Anglian Water of any new Joint Venture to which the Security Trustee and each Financial Guarantor has consented (such consent not to be unreasonably withheld) pursuant to the terms of the CTA and the operation by or on behalf of Anglian Water of that joint venture in accordance with the criteria set out in the CTA and, in relation to any Existing Joint Venture, the above-mentioned terms do not apply;

**“Permitted Lease Termination”**

means any termination of the leasing (or the prepayment of Rentals arising by reason of such termination) of all or any part of the Equipment in the following circumstances:

- (a) *Total Loss*: Pursuant to Clause 7.2 of the Mercantile Existing Finance Lease, Clause 7.2 of the D-LAF Existing Finance Lease, Clause 10(A) of the Deutsche Bank Existing Finance Lease, Clause 6 of the DrKW Finance Existing Finance Lease and Clause 6 of the DrKW Industrial Finance Existing Finance Lease or any other provision of a Finance Lease whereby the leasing of all or any part of the Equipment thereunder will terminate following a total loss of such Equipment save that Anglian Water or the Issuer (as applicable) will not make payment to the relevant Finance Lessor of any sums due and payable under the relevant Finance Lease in respect of such total loss if (i) an Acceleration of Liabilities has occurred or (ii) a Default Situation is subsisting or would occur as a result of such payment;
- (b) *Illegality*: Pursuant to Clause 10(E)(i) of the Deutsche Bank Existing Finance Lease, or any other provision of a Finance Lease which permits the relevant Finance Lessor to terminate the leasing of the Equipment thereunder and to require payment of a termination sum or sums where it is unlawful for such Finance Lessor to continue to lease the relevant Equipment save that Anglian Water or the Issuer (as applicable) will not make payment to the relevant Finance Lessor of any sums due and payable under the Finance Lease in respect of such circumstances if either (i) an

Acceleration of Liabilities has occurred or (ii) a Default Situation is subsisting or would occur as a result of such payment; and

- (c) *Voluntary Prepayment/Termination:* Pursuant to Clause 11.3 of the Mercantile Existing Finance Lease, Clause 11.3 of the D-LAF Existing Finance Lease, Clause 10(B) of the Deutsche Bank Existing Finance Lease, Clause 2.2 of the DrKW Industrial Finance Existing Finance Lease, Clause 2.2. of the DrKW Finance Existing Finance Lease and any other provision of a Finance Lease whereby Anglian Water or the Issuer (as applicable) will be entitled to voluntarily terminate (and require payment of a termination sum), or prepay the Rentals due to, the leasing of certain Equipment under such Finance Lease provided that (i) no Acceleration of Liabilities has occurred or (ii) no Default Situation is subsisting or would occur as a result of such prepayment or termination;

**“Permitted New Non-Statutory Business”**

means any business other than the Regulated Business, and Permitted Existing Non-Statutory Business provided that (a) such business: (i) requires the utilisation of assets or resources that are already owned or controlled by Anglian Water; and (ii) is prudent in the context of the overall business of Anglian Water and continues to be prudent for the duration of that Permitted New Non-Statutory Business; and (iii) is not reasonably likely to be objected to by the DGWS; and (iv) falls within the Permitted Non-Statutory Business Limits applicable to Permitted New Non-Statutory Business and, (b) all material risks related thereto are fully insured and (c) such business does not give rise to any material actual or contingent liabilities for Anglian Water that are not properly provided for in its financial statements;

**“Permitted Non-Statutory Business”**

means Permitted Existing Non-Statutory Business and Permitted New Non-Statutory Business;

**“Permitted Non-Statutory Business Limits”**

means, in respect of Permitted Non-Statutory Business, that the aggregate Non-Regulatory Allowable Expense in any Test Period does not exceed 2.5 per cent. of Cash Expenses of Anglian Water in that period;

**“Permitted Security Interest”**

means:

- (1) any security interest created by any Obligor that is:
  - (a) a Security Interest created under the Security Documents or contemplated by the Finance Documents;
  - (b) any Security Interest specified in Schedule 12 of the CTA as set out in Section 7.6, “*Financing Structure – Cash Management*”, if the principal amount thereby secured is not increased;
  - (c) a Security Interest comprising a netting or set-off arrangement entered into by a member of the Anglian Water Services Financing Group in the ordinary course

- of its banking arrangements for the purpose of netting debit and credit balances;
- (d) a right of set-off, banker's liens or the like arising by operation of laws or by contract by virtue of the provision of any overdraft facility and like arrangements arising as a consequence of entering into arrangements on the standard terms of any bank providing an overdraft;
  - (e) any Security Interest arising under statute or by operation of law in favour of any government, state or local authority in respect of taxes, assessments or government charges which are being contested by the relevant member of the Anglian Water Services Financing Group in good faith and with a reasonable prospect of success;
- (2) any security interest created by either Anglian Water or the Issuer that is:
- (a) a security interest comprising a netting or set-off arrangement entered into under any hedge arrangement entered into in accordance with the Hedging Policy where the obligations of other parties thereunder are calculated by reference to net exposure thereunder (but not any netting or set-off relating to such hedge arrangement in respect of cash collateral or any other Security Interest except as otherwise permitted hereunder);
  - (b) a lien in favour of any bank over goods and documents of title to goods arising in the ordinary course of documentary credit transactions entered into in the ordinary course of trade;
  - (c) a Security Interest created over shares and/or other securities acquired in accordance with the CTA held in any clearing system or listed on any exchange which arise as a result of such shares and/or securities being so held in such clearing system or listed on such exchange as a result of the rules and regulations of such clearing system or exchange;
  - (d) a Security Interest approved by the Security Trustee, the holder of which has become a party to the STID;
- (3) any security interest that is created by Anglian Water that is:
- (a) a Security Interest over or affecting any asset acquired on arm's length terms after the date hereof and subject to which such asset is acquired, if:
    - (i) such Security Interest was not created in contemplation of the acquisition of such asset;
    - (ii) the amount thereby secured has not been increased in contemplation of, or since the date of, the acquisition of such asset by a member of the Anglian Water Services Financing Group; and

- (iii) unless such Security Interest falls within any of Paragraphs (d) to (h) below and (A) such Security Interest is removed or discharged within three months of the date of acquisition of such asset; or (B) the holder thereof becomes party to the STID;
- (b) a Security Interest arising in the ordinary course of business and securing amounts not more than 90 days overdue or if more than 90 days overdue, the original deferral was not intended to exceed 90 days and such amounts are being contested in good faith;
- (c) a Security Interest arising under or contemplated by any Finance Leases, hire purchase agreements, conditional sale agreements or other agreements for the acquisition of assets on deferred purchase terms (other than the Existing Finance Leases) where the counterparty becomes party to the STID;
- (d) a right of set-off existing in the ordinary course of trading activities between Anglian Water and its suppliers or customers;
- (e) a lien arising under statute or by operation of law (or by agreement having substantially the same effect) and in the ordinary course of business provided that such lien is discharged within 30 days of any member of the Group becoming aware that the amount owing in respect of such lien has become due;
- (f) a Security Interest arising on rental deposits in connection with the occupation of leasehold premises in the ordinary course of business; or
- (g) in addition to any Security Interests subsisting pursuant to the above any other Security Interests provided that the aggregate principal amount secured by such Security Interests does not at any time exceed £10,000,000 (or its equivalent) (indexed),

to the extent and for so long, in each case, as the creation or existence of such Security Interest would not contravene the terms of the Instrument of Appointment, the WIA or any requirement under the Instrument of Appointment or the WIA;

**“Permitted Tax Loss Transaction”**

means any surrender of tax losses or agreement relating to tax benefit or relief (including for the avoidance of doubt an election under Section 171 A Taxation of Chargeable Gains Act 1992) or other agreement relating to tax between:

- (a) an Obligor (other than Anglian Water or the Issuer if, in either case, it is the company making the surrender or providing the benefit or relief) and any other member of the Anglian Water Services Financing Group; or
- (b) Anglian Water or the Issuer and any other member of the Anglian Water Services Financing Group or an Obligor and any other member of the AWG Group (not being a member of the Anglian Water Services Financing Group) provided that:

- (i) a payment is made by the company receiving the benefit, tax loss or relief made available under a transaction pursuant to paragraph (b) above (the “**Recipient Company**”) which is equal to the tax saved by the Recipient Company; and
- (ii) the payment for any such benefit, tax loss or relief is made within 30 days of the claim being made by the Recipient Company to include the benefit, tax loss or relief in the tax return (whether the tax return originally filed or an amendment to that tax return) it files with the HM Revenue & Customs;

“**Permitted Volume Trading Arrangements**” means:

- (a) (for the period 12 months from the Effective Date only) contracts entered into by Anglian Water with suppliers for the supply of goods and services to the AWG Group and the Anglian Water Services Financing Group on terms that discounts are available as a result of such arrangements provided that any member of the AWG Group making use of such arrangements agrees to reimburse and indemnify the Anglian Water Services Financing Group for any amounts payable by the Anglian Water Services Financing Group to such suppliers as a result of that member of the AWG Group making use of such arrangements; and
- (b) from the Effective Date, contracts entered into by the AWG Group with suppliers for the supply of goods and services to the AWG Group and the Anglian Water Services Financing Group on terms that discounts are available as a result of such arrangements, provided that any Obligor making use of such arrangements will reimburse the AWG Group for any Financial Indebtedness by way of amounts payable by the AWG Group to such supplier as a result of such Obligor making use of such arrangements;

“**Potential Event of Default**”

means an event (other than in any Hedging Agreement, where “Potential Event of Default” has the meaning given to it in that Hedging Agreement) which would be (with the expiry of a grace period, the giving of notice or the making of any determination under the Finance Documents or any combination of them), an Event of Default;

“**Potential Trigger Event**”

means an event which would be (with the expiry of any relevant grace period or the giving of notice or any combination thereof) if not remedied or waived become a Trigger Event;

“**Premium Letter**”

means the letter or other agreement between a Financial Guarantor and one or more of the Obligors setting the terms on which premia are payable in relation to one or more Bond Policies issued or to be issued by that Financial Guarantor;

“**Pre-Test Period**”

means the period from the Effective Date up to 31 March 2003;

<b>“Principal Paying Agent”</b>	means Deutsche Bank AG, London Branch as principal paying agent under the Agency Agreement, or its successors thereto;
<b>“Procurement Plan”</b>	means the plan for the procurement of services which Anglian Water will prepare pursuant to the Licence as modified;
<b>“Programme”</b>	means the €10 billion global secured medium term note programme established by the Issuer and listed on the Market;
<b>“Programme Agreement”</b>	means the agreement dated on or about 23 September 2005 between the Issuer, the Obligors and the Dealers named therein (or deemed named therein) concerning the purchase of Bonds to be issued pursuant to the Programme together with any agreement for the time being in force amending, replacing, novating or modifying such agreement and any accession letters and/or agreements supplemental thereto;
<b>“Projected Operating Expenditure”</b>	means at any time, the operating expenditure projected in the operating budget for the Test Period in which such date falls;
<b>“Protected Land”</b>	means (as the term is defined in the WIA) any land which, or any interest or right in or over land which: <ul style="list-style-type: none"> <li>(a) was transferred to that Regulated Company in accordance with a scheme under Schedule 2 to the Water Act 1989 or, where that company is a statutory water company, was held by that company at any time during the financial year ending 31 March 1990;</li> <li>(b) is or has at any time on or after 1 September 1989 been held by that company for the purposes connected with the carrying out of its functions as a water undertaker or sewerage undertaker; or</li> <li>(c) has been transferred to that company in accordance with a scheme under Schedule 2 to the WIA from another company in relation to which that land was protected when the other company held an Instrument of Appointment;</li> </ul>
<b>“Public Procurement Rules”</b>	means public procurement rules of the United Kingdom (including the Utilities Contracts Regulations 1996 (SI 1996/2911)) and of the European Communities (including Directive 2004/17/EC) affecting the water and sewerage sector and including any jurisprudence of the courts of the United Kingdom and of the European Communities and decisions of the European Commission in respect of such rules;
<b>“Qualifying Class A Debt”</b>	means the aggregate Outstanding Principal Amount of Class A Debt to be voted by the Class A DIG Representatives;
<b>“Qualifying Class A Debt Provider”</b>	means a provider of Qualifying Class A Debt;
<b>“Qualifying Class B Debt”</b>	means the aggregate Outstanding Principal Amount of Class B Debt to be voted by the Class B DIG Representatives;
<b>“Qualifying Class B Debt Provider”</b>	means a provider of Qualifying Class B Debt;
<b>“Qualifying Debt”</b>	means the Qualifying Class A Debt or the Qualifying Class B Debt, as the context requires;
<b>“Qualifying Debt Provider”</b>	means a provider of Qualifying Debt;

<b>“QIBs”</b>	means a “qualified institutional buyer” within the meaning of Rule 144A under the Securities Act;
<b>“RAG 5”</b>	means Regulatory Accounting Guidelines 5 “Transfer pricing in the water industry”, version 5.03;
<b>“Rating Agencies”</b>	means Fitch, Moody’s and S&P and any further or replacement rating agency appointed by the Issuer with the approval of the Security Trustee (acting upon the instructions of the Majority Creditors) to provide a credit rating or ratings for the Class A Debt and the Class B Debt and shadow ratings in respect of Class A Wrapped Debt and Class B Wrapped Debt for so long as they are willing to provide credit ratings generally (and <b>“Rating Agency”</b> means any one of them);
<b>“Rating Confirmation on Change of Control”</b>	means, in respect of a UK Holdco Change of Control, confirmation from any two Rating Agencies that the shadow rating of the Class A Wrapped Bonds will not be downgraded to BBB+ in the case of Fitch and S&P or, as the case may be, Baa1 in the case of Moody’s, or below;
<b>“Rating Requirement”</b>	means confirmation from any two Rating Agencies that, in respect of any matter where such confirmation is required, that the shadow rating is in the case of the Class A Wrapped Debt, A-by Fitch and S&P and A3 by Moody’s or above and in the case of the Class A Unwrapped Debt, is A- by Fitch and S&P and A3 by Moody’s or above;
<b>“RAV” or “Regulated Asset Value”</b>	means, in relation to any date, the regulated asset value for such date as last determined and notified to Anglian Water by the DGWS at the most recent Periodic Review or IDOK or other procedure through which in future the DGWS may make such determination on an equally definitive basis to that of a Periodic Review or IDOK (interpolated as necessary and adjusted as appropriate for Out-turn Inflation);
<b>“Receipt”</b>	means a receipt attached on issue to a definitive Bearer Bond redeemable in instalments for the payment of an instalment of principal and includes any replacements for Receipts issued pursuant to Condition 15 of the Conditions;
<b>“Receiptholders”</b>	means the several persons who are for the time being holders of the Receipts;
<b>“Receipts Account”</b>	means the joint account of Anglian Water and the Issuer titled “Receipts Account” held at the Account Bank and includes any sub-account relating to that account and any replacement account from time to time;
<b>“Registered Bonds”</b>	means those of the Bonds which are in registered form;
<b>“Registered Global Bonds”</b>	means a Rule 144A Global Bond and/or a Regulation S Global Bond;
<b>“Registrar”</b>	means Deutsche Bank Trust Company Americas, which will act as registrar and will provide certain registrar services to the Issuer in respect of Registered Bonds;
<b>“Regulated Business”</b>	means the business of a “relevant undertaker” (as that term is defined in the WIA) in the United Kingdom carried out by Anglian Water;



<b>“Regulated Company”</b>	means one of the 10 water and sewerage companies and 16 water only companies in England and Wales subject to the regulatory regime contained in the WIA, together the <b>“Regulated Companies”</b> (except as otherwise stated in Chapter 11);
<b>“Regulation S”</b>	means Regulation S under the Securities Act;
<b>“Regulation S Global Bond”</b>	means a global bond in registered form comprising some or all of the Registered Bonds of the same Series sold outside the United States in reliance on Regulation S under the Securities Act;
<b>“Regulatory Information”</b>	means the regulatory accounts Anglian Water is required to submit to Ofwat which are filed in June of each year;
<b>“Relevant Change of Circumstance”</b>	has the same meaning as in Part IV of Condition B of the Licence;
<b>“Remedial Plan”</b>	means any remedial plan agreed by Anglian Water and the Security Trustee under Part 2 of Schedule 6 (Trigger Events) of the CTA as more particularly described in Section 7.5.8(ii), <i>“Financing Structure – Common Terms Agreement – Trigger Event Consequences – Further Information and Remedial Plan”</i> ;
<b>“Rental”</b>	means any scheduled payment of rental, periodic charge or equivalent sum under a Finance Lease;
<b>“Requisite Ratings”</b>	means together the Minimum Short-term Rating and the Minimum Long-term Rating;
<b>“Reserved Matters”</b>	means the rights of the Secured Creditors set out in Section 7.3.20, <i>“Financing Structure – Intercreditor Arrangements – Reserved Matters”</i> ;
<b>“Restricted Payment”</b>	means any Distribution or Customer Rebate other than: <ul style="list-style-type: none"> <li>(a) to the extent required to make any payment under an Authorised Credit Facility in accordance with the provisions of the CTA and the STD, a payment by Anglian Water under the Intercompany Loan Arrangements; or</li> <li>(b) a payment made under a Permitted Tax Loss Transaction; or</li> <li>(c) a UK Holdco Debt Service Distribution;</li> </ul>
<b>“Rolling Average Period”</b>	means on each Calculation Date the Test Period ending on 31 March that falls in the same calendar year as that Calculation Date and the next subsequent two consecutive Test Periods, save that, where the test comes to be calculated at a time when information is not available in respect of any forward looking Test Period (as a result of the DGWS’s determination of price limits for a Periodic Review not having been published in draft or final form) then such Rolling Average Period will be the three 12 month periods which run consecutively backwards and/or forwards from such Calculation Date for which such information is available for the last Test Period in such calculation;
<b>“RPI”</b>	means the United Kingdom Retail Price Index;

<b>“Rule 144A Global Bond”</b>	means a global bond in registered form comprising some or all of the Registered Bonds of the same Series sold to QIBs in reliance on Rule 144A under the Securities Act;
<b>“SDRT”</b>	means stamp duty reserve tax;
<b>“Secretary of State”</b>	means one of Her Majesty’s principal secretaries of state;
<b>“Secured Creditor Representative”</b>	means: <ul style="list-style-type: none"> <li>(a) in respect of the Bondholders (other than holders of the USPP 2001 Bonds), the Bond Trustee;</li> <li>(b) in respect of the Original Lenders under the Initial Authorised Credit Facility Providers, Barclays Bank PLC (as agent);</li> <li>(c) in respect of the Original Lenders under the Bridging Facility Agreement, Barclays Bank PLC (as agent);</li> <li>(d) in respect of the Intercompany Loan Arrangements, the Security Trustee (on behalf of the Issuer);</li> <li>(e) in respect of any Liquidity Facility Provider, the Liquidity Facility Agent; and</li> <li>(f) in respect of any Additional Secured Creditor, the representative of such Additional Secured Creditor (if any) appointed as its Secured Creditor Representative under the terms of the relevant Finance Document and named as such in the relevant Accession Memorandum;</li> </ul>
<b>“Secured Creditors”</b>	means the Security Trustee (in its own capacity and on behalf of the other Secured Creditors), the Bond Trustee (in its own capacity and on behalf of the Bondholders (other than the USPP 2001 Bondholders)), the Bondholders, the Initial Financial Guarantor, the Existing Finance Lessors, the Existing Hedge Counterparties, the Issuer, the Initial Authorised Credit Facility Agent, the Initial Authorised Credit Facility Arranger, the Original Lenders, the Bridging Facility Agent, the Bridging Facility Arranger, the Debt Service Reserve Liquidity Facility Provider, the Liquidity Facility Agent, the O&M Reserve Facility Provider, the Cash Manager (other than when the Cash Manager is Anglian Water), the Agent Bank, the Principal Paying Agent, the Registrar, the Exchange Agent, the Transfer Agent, the USPP Paying Agent and any Additional Secured Creditors;
<b>“Secured Liabilities”</b>	means all present and future sums, liabilities and obligations whatsoever (actual or contingent) payable, owing, due or incurred by an Obligor to the Secured Creditors (or any of them) under any Finance Document;
<b>“Securities Act”</b>	means the United States Securities Act of 1933, as amended;
<b>“Security”</b>	means the security constituted by the Security Documents including any guarantee or obligation to provide cash collateral or further assurance thereunder;
<b>“Security Agreement”</b>	means the deed of charge and guarantee executed in favour of the Security Trustee by each of the Obligors on 30 July 2002;

<b>“Security Assets”</b>	means all property, assets, rights and undertakings the subject of the Security created by the Obligors pursuant to any Security Document;
<b>“Security Documents”</b>	means: <ul style="list-style-type: none"> <li>(a) the Security Agreement;</li> <li>(b) the STID; and</li> <li>(c) any other document evidencing or creating security over any asset of an Obligor to secure any obligation of any Obligor to a Secured Creditor under the Finance Documents;</li> </ul>
<b>“Security Interest”</b>	means: <ul style="list-style-type: none"> <li>(a) any mortgage, pledge, lien, charge, assignment, or hypothecation, or other encumbrance securing any obligation of any person;</li> <li>(b) any arrangement under which money or claims to money, or the benefit of, a bank or other account may be applied, set off or made subject to a combination of accounts so as to effect discharge of any sum owed or payable to any person; or</li> <li>(c) any other type of preferential arrangement (including any title transfer and retention arrangement) having a similar effect;</li> </ul>
<b>“Security Trustee”</b>	means Deutsche Trustee Company Limited or any successor appointed pursuant to the STID;
<b>“Senior Average PMICR”</b>	means the sum of the ratios of Net Cash Flow less the greater of (a) the aggregate of CCD and IRC and (b) Capital Maintenance Expenditure, to Senior Debt Interest for each of the Test Periods comprised in a Rolling Average Period divided by 3;
<b>“Senior Debt”</b>	means all Class A Debt and Class B Debt and any other debt ranking in priority to subordinated debt of any member of the Anglian Water Services Financing Group;
<b>“Senior Debt Interest”</b>	means, in relation to any Test Period and without double counting, an amount equal to the aggregate of all interest paid, due but unpaid or in respect of forward looking ratios, payable (whether or not payable within the terms of the Finance Documents) on the Issuer’s and/or Anglian Water’s obligations under and in connection with all Class A Debt and Class B Debt, all premia paid, due but unpaid or, in respect of forward looking ratios, payable to any Financial Guarantor and adjusted Lease Reserve Amounts or Lease Reserve Amounts paid, due but unpaid or in respect of forward looking ratios, payable on the Issuer’s and/or Anglian Water’s obligations under and in connection with all Class A Debt and Class B Debt in each case during such Test Period (after taking account of the impact on interest rates of all and related Hedging Agreements then in force) (excluding all indexation of principal to the extent it has been included in such interest or other amounts and all other costs incurred in connection with the raising of such Class A Debt and/or Class B Debt),

and excluding amortisation of the costs of issue of any Class A Debt and Class B Debt within such Test Period less all interest received or in respect of forward looking ratios receivable by any member of the Anglian Water Services Financing Group from a third party during such Test Period;

**“Senior ICR”**

means the ratio of Net Cash Flow for each Test Period to Senior Debt Interest for each of the same Test Periods;

**“Senior Net Indebtedness”**

means, as at any date, all the Issuer’s and Anglian Water’s nominal debt outstanding under and in connection with any Class A Debt and Class B Debt (other than pursuant to tranche B of the Initial Authorised Loan Agreement) and any nominal amounts of Financial Indebtedness falling within paragraph (e) of the definition of Permitted Financial Indebtedness including (in each case) all indexation accrued but unpaid (after taking account of the impact on interest rates of all related Hedging Agreements then in force) on any such liabilities which are indexed together with any interest due and unpaid (after taking account of the impact on interest rates of all related Hedging Agreements then in force) and less the value of all Authorised Investments and other amounts standing to the credit of any Account other than the Customer Payment Account or the Distributions Accounts (where such debt is denominated other than in Sterling, the nominal amount outstanding will be calculated (i) in respect of debt with associated Currency Hedging Agreements, by reference to the applicable hedge rates; or (ii) in respect of debt with no associated Currency Hedging Agreements, by reference to the Exchange Rate);

**“Senior PMICR”**

means the ratio of Net Cash Flow less the greater of (a) the aggregate CCD and IRC and (b) Capital Maintenance Expenditure for each Test Period to Senior Debt Interest for each of the same Test Periods for that period;

**“Senior RAR”**

means the ratio of Senior Net Indebtedness to RAV;

**“Series”**

means a Tranche of Bonds together with any further Tranche or Tranches of Bonds which are (i) expressed to be consolidated and form a single series and (ii) identical in all respects (including as to listing) except for their respective Issue Dates, Interest Commencement Dates and/or Issue Prices;

**“Shipwreck Clause”**

means a clause which may be contained in the licence of a Regulated Company and which is contained in the Licence of Anglian Water at Part IV of Condition B, pursuant to which the Regulated Company may, if so permitted by the conditions of its licence, request price limits to be reset if the Regulated Business either (i) suffers a substantial adverse effect which could not have been avoided by prudent management action or (ii) enjoys a substantial favourable effect which is fortuitous and not attributable to prudent management action;

**“Special Administration”**

means the insolvency process specific to Regulated Companies under Sections 23-26 of the WIA;

**“Special Administration Order”**

means an order of the High Court under Sections 23-25 of the WIA under the insolvency process specific to Regulated Companies;

<b>“Special Administration Petition Period”</b>	means the period beginning with the presentation of the petition for Special Administration under Section 24 of the WIA and ending with the making of a Special Administration Order or the dismissal of the petition;
<b>“Special Administrator”</b>	means the person appointed by the High Court under Sections 23-25 of the WIA to manage the affairs, business and property of the Regulated Company during the period in which the Special Administration Order is in force;
<b>“Special Distribution”</b>	means a Distribution: <ul style="list-style-type: none"> <li>(a) that is made out of amounts in excess of Net Cash Flow, less any Distribution which has already been paid in respect of that Financial Year, generated in the 12 months to the most recently occurring 31 March or generated in the six months up to 30 September (as the case may be) less Capital Maintenance Expenditure, less Senior Debt Interest, less any amounts required to restore the Liquidity Facilities to the required levels (in each case calculated for the same period); or</li> <li>(b) that is not an Ordinary Distribution;</li> </ul>
<b>“Standard &amp; Poor’s” or “S&amp;P”</b>	means Standard & Poor’s Ratings Services, a Division of the McGraw-Hill Companies Inc.;
<b>“Standby Drawing”</b>	means a drawing made under a Liquidity Facility Agreement as a result of a downgrade of a Liquidity Facility Provider below the required ratings or in the event that the Liquidity Facility Provider fails to renew its commitment on the expiry of its term;
<b>“Standstill”</b>	means, as provided for in the STID, a standstill of claims of the Secured Creditors against Anglian Water and the Issuer immediately upon notification to the Security Trustee of the occurrence of an Event of Default;
<b>“Standstill Event”</b>	means an event giving rise to a Standstill in accordance with the STID;
<b>“Standstill Period”</b>	means a period during which a standstill arrangement is subsisting;
<b>“Statutory Accounts”</b>	means the statutory accounts which Anglian Water is required to prepare in compliance with the Companies Act;
<b>“STID”</b>	means the security trust and intercreditor deed dated 30 July 2002 between the Obligors and the Secured Creditors pursuant to which the Security Trustee holds the Security on trust for the Secured Creditors and the Secured Creditors agree to certain intercreditor arrangements;
<b>“STID Directions Request”</b>	means a written notice of each STID Proposal sent by the Security Trustee to the Secured Creditors pursuant to the STID;
<b>“STID Proposal”</b>	means a proposal pursuant to the STID requiring a Majority Creditor decision and the consent of any Secured Creditor having an Entrenched Right in respect of such proposal;
<b>“Subordinated Authorised Loan Amounts”</b>	means, in relation to any Authorised Credit Facility, the aggregate of any amounts payable by the Issuer to the relevant

Authorised Credit Provider on an accelerated basis as a result of illegality on the part of the Authorised Credit Provider or any other amounts not referred to in any other paragraph of the Payment Priorities;

**“Subordinated Coupon Amounts”**

means, in respect of any Floating Rate Bonds, any amounts (other than deferred interest) by which the margin on the Coupon on such Bonds exceeds the initial margin on the Coupon on such Bonds as at the date on which such Bonds were issued;

**“Subordinated Debt”**

means any secured Financial Indebtedness that is fully subordinated, in a manner satisfactory to the Security Trustee and each Financial Guarantor, to the Class A Debt and Class B Debt and where the relevant credit provider has acceded to the Common Terms Agreement and the STID;

**“Subordinated Liabilities”**

means, all present and future liabilities (actual or contingent) payable or owing by an Obligor to another Obligor whether or not matured and whether or not liquidated other than (until the Security Trustee directs otherwise) any amounts payable or owing by UK Holdco to Anglian Water under the UK Holdco/Anglian Water Loan and any amounts payable or owing under the Anglian Water Loan Notes or the Issuer/Anglian Water Loan Agreement;

**“Subordinated Liquidity Facility Amounts”**

means, in relation to any Liquidity Facility, the amount by which the cost of regulatory compliance or the interest rate payable exceeds what it was on the Issue Date and the aggregate of amounts payable by the Issuer to the relevant Liquidity Provider on an accelerated basis as a result of illegality, gross up or increased costs on the part of such Liquidity Facility Provider or any other amounts not referred to in any other paragraph of the Payment Priorities;

**“Subordinated O&M Reserve Facility Amounts”**

means, in relation to the O&M Reserve Facility, the aggregate of any amounts payable by the Issuer to the O&M Reserve Facility Provider on an accelerated basis as a result of illegality on the part of the O&M Reserve Facility Provider or any other amounts not referred to in any other paragraph of the Payment Priorities;

**“Talons”**

means the talons (if any) appertaining to, and exchangeable in accordance with the provisions therein contained for further Coupons appertaining to, the definitive Bearer Bonds (other than Zero Coupon Bonds) and includes any replacements for Talons issued pursuant to Condition 15 of the Conditions;

**“Talonholders”**

means the several persons who are for the time being holders of the Talons;

**“Tax Deed of Covenant”**

means the deed of covenant entered into on or about the Effective Date between, *inter alios*, the Security Trustee and the Obligors;

**“Temporary Bearer Global Bond”**

means a temporary global bond comprising some or all of the Bearer Bonds of the same Series issued by the Issuer;

**“Test Period”**

means: (a) the period of 12 months ending on 31 March in the then current year; (b) the period of 12 months starting on 1 April in the same year; (c) each subsequent 12 month period up to the Date Prior; and (d) where the Calculation Date falls

within the 13 month period immediately prior to the Date Prior, includes the 12 month period from the Date Prior;

- “Tier 1 Material Agreement”** means any Tier 1 Material O&M Agreement or a Tier 1 Material Capex Agreement;
- “Tier 2 Material Agreement”** means any Tier 2 Material O&M Agreement or a Tier 2 Material Capex Agreement;
- “Tier 1 Material Capex Agreement”** means any Capex Contract entered into by Anglian Water for the purposes of, or in connection with, Anglian Water carrying out its Regulated Business, where the NPV at the later of (a) the Effective Date or (b) the date at which it is entered into or amended, supplemented or novated, of the agreed target cost payable by Anglian Water under that contract (which in each case has not been terminated or expired in accordance with its terms), is, or would be if such contract was entered into on arm’s length terms and for full value, equal to or greater than £15,000,000 (indexed);
- “Tier 2 Material Capex Agreement”** means any Capex Contract entered into by Anglian Water for the purposes of, or in connection with, Anglian Water carrying out its Regulated Business, where the NPV at the later of (a) the Effective Date or (b) the date at which it is entered into or amended, supplemented or novated, of the agreed target cost payable by Anglian Water under that contract (which in each case has not been terminated or expired in accordance with its terms), is, or would be if such contract was entered into on arm’s length terms and for full value, less than £15,000,000 (indexed) but more than or equal to £5,000,000 (indexed);
- “Tier 1 Material O&M Agreement”** means any Outsourcing Agreement or series of Outsourcing Agreements (taken together) where the annual value of which is equal to or greater than contracts entered into between Anglian Water and any Contractor (or its affiliates) (which in each case has not been terminated or expired in accordance with its terms) exceeds (or would exceed were it entered into on arm’s length terms) 25 per cent. of the Projected Operating Expenditure;
- “Tier 2 Material O&M Agreement”** means any Outsourcing Agreement or series of Outsourcing Agreements (taken together), the annual value of which is equal to or greater than £5,000,000 (indexed), entered into with any Contractor and where the annual value of contracts entered into between Anglian Water and that Contractor (or its affiliates) (which in each case has not been terminated or expired in accordance with its terms) is less than 25 per cent. of the Projected Operating Expenditure;
- “Tranche”** means all Bonds which are identical in all respects (including as to listing);
- “Transaction Documents”** means:
- (a) a Finance Document;
  - (b) a Tier 1 Material Agreement; and
  - (c) any other document designated as such by the Security Trustee and the Issuer;

<b>“Transfer Agent”</b>	means Deutsche Bank AG, London Branch under the Agency Agreement, including any successor thereto;
<b>“Transfer Scheme”</b>	means a transfer scheme under Schedule 2 of the WIA;
<b>“Transferred USPP Bonds”</b>	means those Bonds identified as USPP Bonds in the relevant pricing supplement and issued by the Issuer on the Effective Date in exchange for those of the following bonds previously issued by AWG Group Ltd: <ul style="list-style-type: none"> <li>(a) \$4,000,000 6.71 per cent. bonds due 2006;</li> <li>(b) \$25,000,000 6.57 per cent. bonds due 2009;</li> <li>(c) \$10,000,000 6.54 per cent. bonds due 2008;</li> <li>(d) \$156,000,000 6.84 per cent. bonds due 2013; and</li> <li>(e) \$122,000,000 6.35 per cent. bonds due 2006,</li> </ul> and the USPP 2001 Bonds;
<b>“Treasury Transaction”</b>	means any currency or interest rate purchase, cap or collar agreement, forward rate agreement, interest rate agreement, interest rate or currency or future or option contract, foreign exchange or currency purchase or sale agreement, interest rate swap, currency swap or combined similar agreement or any derivative transaction protecting against or benefiting from fluctuations in any rate or price;
<b>“Trigger Credit Rating”</b>	means each of the credit ratings referred to in Section 7.5.7(ii), <i>“Financing Structure – Common Terms Agreement – Trigger Events – Credit Rating Downgrade”</i> ;
<b>“Trigger Event”</b>	means any of the events or circumstances identified as such in the CTA, as more particularly described in Section 7.5.7, <i>“Trigger Events”</i> ;
<b>“Trigger Event Consequences”</b>	means any of the consequences of a Trigger Event as identified as such in the CTA, as more particularly described in Section 7.5.8, <i>“Financing Structure – Trigger Event Consequences”</i> ;
<b>“Trigger Event Ratio Levels”</b>	means the financial ratios set out in Section 7.5.7(i), <i>“Financing Structure – Common Terms Agreement – Trigger Events – Financial Ratios”</i> ;
<b>“Trigger Event Remedies”</b>	means any remedy to a Trigger Event as identified in the CTA, as more fully particularised in Section 7.5.9, <i>“Financing Structure – Trigger Event Remedies”</i> ;
<b>“UK Holdco”</b>	means Anglian Water Services Holdings Ltd;
<b>“UK Holdco/Anglian Water Loan” and “UK Holdco/AWS Loan”</b>	means the interest-bearing loan made to Anglian Water Services Holdings Ltd by Anglian Water to enable Anglian Water Services Holdings Ltd to pay the consideration to AWG Group Ltd to purchase the shares held by AWG Group Ltd in Anglian Water Services Overseas Holdings Ltd in an amount consistent with the limitations under permitted post closing events;



<b>“UK Holdco Change of Control”</b>	means the occurrence of any of the following events or circumstances or the reasonable likelihood of such events or circumstances happening: <ul style="list-style-type: none"> <li>(a) any person which previously Controls Anglian Water Services Holdings Ltd ceasing to have Control of Anglian Water Services Holdings Ltd; or</li> <li>(b) any person which does not previously Control Anglian Water Services Holdings Ltd obtaining Control of Anglian Water Services Holdings Ltd,</li> </ul> of which any Obligor has actual knowledge;
<b>“UK Holdco Debt Service Distribution”</b>	means a dividend payment declared and paid by Anglian Water and/or Anglian Water Services Overseas Holdings Ltd that meets the criteria specified in Section 7.5.5(iv)(v)(E), “ <i>Covenants – General</i> ” and the payment by Anglian Water Services Holdings Ltd of sums payable to Anglian Water under the UK Holdco/Anglian Water Loan in each Financial Year;
<b>“UK Listing Authority”</b>	means the Financial Services Authority in its capacity as competent authority under the Financial Services and Markets Act 2000, as amended;
<b>“Unwrapped Bonds”</b>	means those Bonds that do not have the benefit of a guarantee from a Financial Guarantor;
<b>“Unwrapped Debt”</b>	means any indebtedness that does not have the benefit of a guarantee from a Financial Guarantor;
<b>“USPP Bonds”</b>	means the USPP 2001 Bonds and those Bonds identified as USPP Bonds in the relevant pricing supplement or Final Terms relating to any Class A Unwrapped Bonds or Class B Unwrapped Bonds issued by the Issuer on or after the Effective Date;
<b>“USPP 2001 Bonds”</b>	means such amount of the Series A 6.57 per cent. Senior Notes due 2005, Series B 6.62 per cent. Senior Notes due 2006, Series C 7.01 per cent. Senior Notes due 2008, Series D 7.13 per cent. Senior Notes due 2009 and Series E 7.23 per cent. Senior Notes due 2011, all issued by Anglian Water in July 2001 which remained outstanding immediately after the Effective Date;
<b>“USPP Bondholders”</b>	means the holders of USPP Bonds;
<b>“USPP Paying Agent”</b>	means Deutsche Bank Trust Company Americas or any successor thereto;
<b>“UV”</b>	means ultra-violet;
<b>“UWWTD”</b>	means the Urban Waste Water Treatment Directive;
<b>“VAT”</b>	means value added tax;
<b>“Voted Qualifying Class A Debt”</b>	means the aggregate Outstanding Principal Amount of Class A Debt voted by the Class A DIG Representatives in accordance with the applicable provisions of the STID as part of the Class A DIG;

<b>“Voted Qualifying Class B Debt”</b>	means the aggregate Outstanding Principal Amount of Class B Debt voted by the Class B DIG Representatives in accordance with the applicable provisions of the STID as part of the Class B DIG;
<b>“Voted Qualifying Debt”</b>	means the Voted Qualifying Class A Debt or the Voted Qualifying B Debt, as the context requires;
<b>“Water Act”</b>	means the United Kingdom Water Act 2003;
<b>“Water Authorities”</b>	means the 10 regional public sector water authorities supplying water and sewerage services in England and Wales prior to privatisation in 1989;
<b>“Water Quality Regulations”</b>	means the United Kingdom Water Supply (Water Quality) Regulations 1989, as amended, inter alia, by the Water Supply (Water Quality) Regulations 2000 and the Water Supply (Water Quality) (Amendment) Regulations 2001;
<b>“WIA”</b>	means the United Kingdom Water Industry Act 1991 (as amended by subsequent United Kingdom legislation, including the Competition and Service (Utilities) Act 1992, the Water Industry Act 1999 and the Water Act); and
<b>“WRA”</b>	means the United Kingdom Water Resources Act 1991, as amended by subsequent legislation including the United Kingdom Environment Act 1995 and the Water Act;
<b>“WSRA”</b>	means the United Kingdom Government’s Water Services Regulation Authority;
<b>“Wrapped Bonds”</b>	means those bonds that have the benefit of a guarantee from a Financial Guarantor;
<b>“Wrapped Debt”</b>	means any indebtedness that has the benefit of a guarantee from a Financial Guarantor;
<b>“Wrongful Payment”</b>	means any Distributions (otherwise than pursuant to an agreement, contract or other similar arrangement) in breach of Section 7.5.5(iv)(v), “ <i>Financing Structure – Common Terms Agreement – Covenants – General</i> ”, which are in an aggregate amount of £500,000 (indexed) or less in each Financial Year; and
<b>“Zero Coupon Bond”</b>	means a Bond on which no interest is payable.

## APPENDIX

### OFWAT LETTER

The following extract is taken from the letter to the Managing Directors of all Regulated Companies from the present DGWS issued on 31 January 2001, in which he indicated the general principles he would follow in carrying out periodic reviews.

#### **The Duties of the Director General of Water Services and the Regulatory Framework**

##### **1. The Director's duties**

The Director's primary duties, as set out in the Water Industry Act 1991 (the "Act"), are to act in a manner that he considers best calculated to secure that the functions of Appointees are properly carried out and that Appointees are able to finance the proper carrying out of those functions. The Director also has duties to protect the interests of customers, to promote economy and efficiency and to facilitate competition and has certain environmental and recreational duties.

##### **2. The Director's approach to Periodic Reviews**

- (i) The Director is required to reset price limits at five yearly reviews. In doing so, he must have regard to his primary duties. Although the detailed methodology is not set out either in the Act or in companies' licence conditions, Ofwat has sought to conduct the reviews in an open and transparent manner and will continue to do so. The principles and methodology that have been adopted have been subject to wide consultation and consequent refinement.
- (ii) Prices are set so that revenues cover the cost of the efficient provision of operations and capital investment, and allow a reasonable return on capital. The ability of the Appointee to maintain an adequate level and trend of critical financial indicators is also taken into account. This is with a view to ensuring that, provided the Appointee is efficiently managed and financed, it will remain able to finance its functions (including new investment), readily and at reasonable cost. Where appropriate, account is taken of the Appointee's duty to maintain investment grade credit ratings.
- (iii) Ofwat has taken 'capital' to be the 'Regulatory Capital Value' ("RCV") of the Appointed Business. The criteria for determining the RCV are set out in Setting price limits for water and sewerage services: *The framework and business planning process for the 1999 Review (February 1998)* and updated in MD145, *The framework for setting prices*, published in March 1999. The approach taken at the 1999 Periodic Review built on that adopted at the 1994 review. The initial capital value, as placed on the holding companies of the Appointees by the financial markets in 1989, was adjusted for net new allowable capital expenditure and depreciation charges since then, including at the 1999 review an adjustment to reflect past capital efficiencies, to arrive at the RCV. The implications of subsequent capital transactions including mergers and takeovers have not been taken into account when considering the RCV at Periodic Reviews.
- (iv) At the 1999 Review the return on capital allowed was based on an assessment of the real post-tax weighted average cost of debt and equity for an efficiently-financed stand-alone listed water and sewerage company. This assessment was based on the market's view of a forward-looking cost of capital. Amongst other things, this assessment reflected Ofwat's perception that investors, despite the significant capital investment requirements, viewed the water industry as relatively low risk and that it represents a lower risk than the United Kingdom stock market as a whole.
- (v) Ofwat included in the allowed return at the 1999 Periodic Review an adjustment to reflect the prudently incurred cost of long-term fixed rate debt. This adjustment was made to take into account a change in the 1999 methodology from the glidepath of returns on existing assets set in 1994. Ofwat also placed greater emphasis on current market evidence of the cost of capital rather than on longer term historical averages. There can, however, be no guarantee that such financing costs will be passed on to customers at future reviews since similar circumstances are unlikely to occur. The Director will be guided primarily by consideration of the Appointee's relative efficiency in managing its financial affairs, just as he will be guided by this consideration with regard to other areas of costs. An Appointee that fails to maintain the flexibility to respond to changing market conditions risks being judged relatively inefficient.

- (vi) In setting prices, either at a five yearly Periodic Review or if a company applies for an Interim Determination of price limits, the Director must make judgements as to the efficient level of costs to assume. A wide range of comparative techniques has been used to inform these judgements since privatisation.
- (vii) Ultimately, the Director has discretion over the ways in which price limits are set and he needs to keep under review the regulatory framework in the light of all relevant developments. Consequently, whilst there can be no assurance that future Periodic Reviews will be conducted in the same manner as past ones, nevertheless, the principles underlying the present price review methodology have been developed over the past ten years and have proved robust. For the next Periodic Review, Ofwat will, of course, take into account the conclusions of the recent Competition Commission reviews in respect of Mid Kent Water and Sutton & East Surrey Water.

### **3. Regulation between five yearly reviews**

- (i) Companies may seek a change to their price limits between Periodic Reviews under the Interim Determination arrangements set out in their Licences. These can be triggered in defined circumstances, for example, where a new legal obligation is imposed which was not taken into account at the last Periodic Review. These instances have, so far, not been very frequent.
- (ii) A modification to the assessment of materiality for Interim Determinations was published with the Final Determination of price limits for 2000-05. This has now been accepted by the majority of companies. The Director believes that this licence modification strengthens the protection available to companies because it includes the effect of revenue loss and operating expenditure over a 15 year horizon in the assessment as to whether the materiality threshold for triggering a price limit adjustment has been met.
- (iii) The Director has proposed in MD167 (31 January 2001) that the provisions commonly known as the 'shipwreck' clause be extended to all companies. The clause enables companies' price limits to be reset between Periodic Reviews if there has been a substantial adverse or favourable effect that could not have been avoided or is not attributable to prudent management action. The clause was (in its original form) included in all companies' licences at privatisation but was removed or revised as part of a review of Condition B of the licence before the 1995 Periodic Review. Less than half of the companies now have the clause in its licence. One company has asked the Director to reinsert this clause in their licence. The Director believes that it is desirable in principle that water companies' licences should not differ unnecessarily and hence has proposed making the modification to all companies' licences.

### **4. Consistency and new ownership structures**

- (i) Following the 1999 Periodic Review a number of companies have explored the possibility of establishing new structural arrangements for the carrying out of their duties as water and sewage undertakers. Companies that choose to structure their business in ways other than the equity-owned, vertically-integrated structure established at privatisation will receive no special or preferential treatment from Ofwat. Licence holders will continue to bear all of the licence obligations of a water and sewerage undertaker. They will continue to be regulated in the same way as other Appointees, and will operate under a price cap and be subject to Periodic Reviews.
- (ii) A consistent approach is particularly important when considering whether licence conditions should be modified from the model which currently applies to the other Appointees. In each case the Director would consider carefully the need for licence modifications and would consult publicly on these.
- (iii) The performance of all companies (in terms of efficiency and customer services) will be judged in a consistent manner, both through the league tables and analysis that Ofwat publishes annually and at Periodic Reviews. The ability to compare companies is an important tool for the regulator of the water and sewerage companies. It is an essential part of the system of incentive regulation and has led to substantial improvements in efficiency since privatisation.
- (iv) Where Appointees have put in place new structural arrangements, the approach at Periodic Reviews will follow that for an equity-owned, vertically integrated Appointee. For example, the approach to RCVs will be assessed similarly and the weighted average cost of capital will be that

which applies to the industry as a whole. The Director will, at the time, take account of the market's view of the cost of capital for the water industry.

- (v) The proposal by a number of companies to separate the ownership of the assets from their operations and to contract out the latter will provide additional information to assist the Director with his assessment of relative efficiency. However, the appropriate level of costs to be assumed within price limits will continue to be assessed on a comparative basis and the existence of competitively tendered prices will not be seen, a priori, as evidence of efficiency nor guarantee that such costs will be fully reflected in price limits.
- (vi) By way of illustration, Ofwat's approach to comparisons of capital programmes has identified widespread differences between companies' unit costs. This is despite these being based upon competitively tendered work or actual costs for capital works. Consequently, at the last Periodic Review, adjustments to capital costs varied from nil to a reduction of 25 per cent.
- (vii) As for all Appointees, Ofwat will ensure that customers' interests continue to be protected after any new structural arrangements are in place through the provisions in the Water Industry Act 1991. This includes, in the last resort, using the powers to apply for the appointment of a Special Administrator in particular circumstances (as set out in Section 5(iv) and 5(v), together with sections 6(iii) and 6(vii)). The main reasons for doing this would be a breach by the company of one of its principal duties in the Act (see sections 47 and 94 of the Act), insolvency or non-compliance with an enforcement order following breach of a licence condition.

## **5. Licence termination**

There are a number of circumstances as provided in the Act in which a particular company could cease to be the licence holder for all or part of its area. These are set out below.

- (i) An Appointee could consent to the making of a replacement Appointment or a Variation, which changes its Water Supply or Sewerage Service Area. In these circumstances the Director has the authority to appoint a new licence holder.
- (ii) An Appointee's Licence could be terminated in the circumstances set out in Condition O of its Licence. These are that it is at least 25 years after the "Transfer Date" (1 September 1989) and 10 years after notice has been served by the Secretary of State (DEFRA). Termination would occur when a successor had been appointed. The power to terminate each Appointee's licence and appoint a successor in these circumstances lies with the Secretary of State although the Director may be authorised to do those things. When required to do so, Ofwat will advise the Secretary of State on the issue of notice of licence termination for any or all undertakers.
- (iii) An Appointee's Licence could be terminated under the provisions of Special Administration. The Secretary of State may apply to the High Court for a Special Administration Order and can also authorise the Director to do so. The main reasons for doing this would be a breach by the Appointee of one of its principal duties in the Act (see sections 37 and 94 of the Act) insolvency or non-compliance with an enforcement order following breach of a licence condition.
- (iv) A Special Administration Order requires the appointment by the High Court of a Special Administrator. The Special Administrator would have responsibility for transferring the water and sewerage business as a going concern to a successor company or companies, under a scheme which must be approved by the Secretary of State, and running the business in the meantime.
- (v) The Act also provides in certain circumstances for the appointment of a new Appointee for part of the existing Appointee's Water Supply or Sewerage Service Area. These appointees are more commonly known as 'Inset Appointments'. These are allowed where the appointment relates to a part of the Appointee's area where no premises are served by the licence holder or the premises are supplied with not less than 100 megalitres of water in any period of twelve months or if the licence holder consents. The Director is authorised to appoint a new licence holder when making Inset Appointments.

## **6. Creditor protection in the event of licence termination**

- (i) In the event of licence termination by agreement or under the circumstances set out in Condition O (see 5(iii) above) the outgoing Appointee should prepare a 'Transfer Scheme', covering the

transfer of property, rights and liabilities to new Appointee(s). The scheme may provide for debt obligations to be transferred to the new Appointee(s). The scheme would have to be agreed by the outgoing Appointee and the new Appointee and approved by the Secretary of State or the Director if authorised.

- (ii) In making an Appointment or Variation replacing the incumbent as the Appointee, the Secretary of State (or Director) would (so far as is consistent with his other duties, particularly those in Section 2 of the Act) have to ensure that the interests of its creditors were not unfairly prejudiced by the transfer terms. This would be addressed through the requirement for approval of the Transfer Scheme.
- (iii) Under Special Administration, the Act provides for the replacement of the Appointee by a successor. In the meantime the Special Administrator must run the business in a manner which protects the interests of shareholders and creditors of the company.
- (iv) The Secretary of State, or with his consent the Director, may approve a Transfer Scheme which moves the Appointed Business into the control of a successor. The Special Administrator would oversee the preparation of the Transfer Scheme.
- (v) There can be no assurance that the transfer following Special Administration could be achieved on terms that enabled creditors of the Appointee to recover amounts due to them in full. The successor Appointee would be subject to the price limits applicable to the original Appointee prior to the transfer becoming effective. Ofwat's duty to protect customers would preclude the granting of price limit relief in such circumstances, unless these were justified by reference to factors other than the Special Administration and the transfer.
- (vi) In addition under Special Administration the Secretary of State may, with Treasury consent, arrange for financial assistance to be provided for the purpose of achieving the transfer of the business and its running in the meantime.
- (vii) Although the protection of creditors is explicit in the Act, no licence has, as yet, been terminated under Condition O, nor has a Special Administration Order been made or sought.

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