Dwr Cymru (Financing) Limited

(incorporated in the Cayman Islands with limited liability with registered number 108127)

Multicurrency programme for the issuance of up to

£3,000,000,000 Guaranteed Asset-Backed Bonds

of which £1,000,000,000 of Series 1 Class A Bonds are unconditionally and irrevocably guaranteed as to scheduled payments of principal and interest pursuant to financial guarantee insurance policies issued by

MBIA Assurance S.A.

(Originally registered on 3 May 1990 with the Nanterre Register of Trade and Companies Currently registered with the Paris Register of Trade and Companies under No. B377883293 (98B05130))

and

£3,000,000,000 Asset-Backed Bonds including up to £200,000,000 Class R Bonds

financing

Dŵr Cymru Cyfyngedig

(incorporated in England and Wales with limited liability with registered number 2366777)

Application has been made to the Luxembourg Stock Exchange to list the bonds (''**Bonds**'') issued under the programme (the ''**Programme**'') during the period of twelve months after the date hereof, and in connection therewith the Luxembourg Stock Exchange has assigned registration number 12556 to the Programme.

Under the Programme, Dwr Cymru (Financing) Limited (the ''**Issuer**'') may, subject to all applicable legal and regulatory requirements, from time to time issue Bonds in bearer and/or registered form (respectively ''**Bearer Bonds**'' and ''**Registered Bonds**''). Copies of each Pricing Supplement (as defined below) will be available (in the case of all Bonds) from the specified office set out below of Bankers Trustee Company Limited as trustee (the ''**Bond Trustee**''), (in the case of Bearer Bonds) from the specified office set out below of each of the Paying Agents (as defined below) and (in the case of Registered Bonds) from the specified office set out below of each of the Registrar and the Transfer Agents (each as defined below).

Details of the aggregate principal amount, interest (if any) payable, the issue price and any other conditions not contained herein, which are applicable to each Sub-Class of each Class of each Series (all as defined below) will be set forth in a pricing supplement (each a ''**Pricing Supplement**'') which will be delivered to the Luxembourg Stock Exchange on or before the relevant date of issue and will be available from Extel Information Centre operated by FT Information Limited at 15 Clere Street, London EC2A 4LJ.

Bonds to be issued under the Programme will be issued in series (each a ''**Series**'') and may be issued in one or more of five classes. The Guaranteed Asset-Backed Bonds will be designated as ''**Class A Bonds**''. The Asset-Backed Bonds will be designated as one of ''**Class B Bonds**'', ''**Class R Bonds**'' ''**Class C Bonds**'' or ''**Class D Bonds**'' (together with the Class A Bonds, each, a ''**Class**''). Each Class may be further divided into sub-classes (each a ''**Sub-Class**'') with each Sub-Class pertaining to, *inter alia*, the currency, interest rate and maturity date of the relevant Sub-Class. Each Sub-Class may be fixed rate, floating rate or index-linked Bonds and may be denominated in sterling, euro, U.S. dollars or other currency, as specified in the relevant Pricing Supplement.

Each Sub-Class of the Class A Bonds, Class B Bonds, Class R Bonds and Class C Bonds to be issued on 10 May 2001, or such other date as the Co-Arrangers and the Issuer may agree, (the ''**Initial Issue Date**'') is expected on issue to have each of the three following credit ratings, and each Sub-Class of such Bonds issued after the Initial Issue Date is expected on issue to have at least two of the three following credit ratings, from the respective credit rating agencies below. None of the Class D Bonds will be assigned a credit rating by such credit rating agencies.

Class	Standard & Poor's	Moody's	Fitch
Class A Bonds	AAA	Aaa	AAA
Class B Bonds	A-	A3	A-
Class R Bonds	A-	A3	A-
Class C Bonds	BBB	Baa3	BBB

The Class A Bonds issued on the Initial Issue Date will be unconditionally and irrevocably guaranteed as to scheduled payments of interest and principal (other than any accelerated or additional amounts and Subordinated Coupon Amounts, as defined below) pursuant to financial guarantee insurance policies (and the endorsements thereto) to be issued by MBIA Assurance S.A. (''**MBIA**'') as set out in Chapter 7. The credit rating of such Class A Bonds will be based solely upon the financial strength of MBIA. None of the Class B Bonds, Class R Bonds, Class C Bonds or Class D Bonds will benefit from a guarantee of MBIA or any other financial institution. Any ratings ascribed to the Bonds reflect only the views of Standard & Poor's, a division of The McGraw-Hill Companies, Inc. (''**Standard & Poor's**''), Moody's Investors Service Limited (''**Moody's**'') and Fitch Ratings Limited (''**Fitch**'' and, together with Standard & Poor's and Moody's, the ''**Rating Agencies**'').

A credit rating is not a recommendation to buy, sell or hold securities and may be subject to revision, suspension or withdrawal at any time by any one or all of the Rating Agencies. A suspension, reduction or withdrawal of the rating assigned to any of the Bonds may adversely affect the market price of such Bonds.

Please see Chapter 5: ''Investment Considerations'' to read about certain factors you should consider before buying any Bonds.

Co-Arrangers for the Programme

Schroder Salomon Smith Barney **The Royal Bank of Scotland**

Dealers

Schroder Salomon Smith Barney **The Royal Bank of Scotland**

Barclays Capital **Lehman Brothers** **Banc of America Securities Limited**

Information Memorandum dated 4 May 2001

IMPORTANT NOTICE

This Information Memorandum should be read and construed with any amendment or supplement hereto and with any other documents incorporated by reference herein and, in relation to any Sub-Class of Bonds, should be read and construed together with the relevant Pricing Supplement.

*The Issuer accepts responsibility for the information contained in or appended to this document except for the MBIA Information and the Glas Information (each as defined below) for which MBIA Assurance S.A. ("**MBIA**") and Glas Cymru Cyfyngedig ("**Glas**") respectively expressly herein assume responsibility. To the best of the knowledge and belief of the Issuer (which has taken all reasonable care to ensure that such is the case), the information contained herein, other than the MBIA Information and the Glas Information, is in accordance with the facts and does not omit anything likely to affect the import of such information.*

*MBIA accepts responsibility for the information contained in Chapter 7: "MBIA and the Bond Policies" and in paragraphs 11 to 15 (inclusive) and 18 of Chapter 15: "General Information" and in the financial statements of MBIA and MBIA Insurance Corporation appended to this Information Memorandum (the "**MBIA Information**"). To the best of the knowledge and belief of MBIA (which has taken all reasonable care to ensure that such is the case), the MBIA Information is in accordance with the facts and does not omit anything likely to affect the import of the MBIA Information. MBIA accepts no responsibility for any other information contained in this Information Memorandum and has not separately verified any such other information.*

*Glas accepts responsibility for the information contained in Chapter 11: "Glas Cymru Cyfyngedig" any statement of Glas's intention with respect to Dŵr Cymru Cyfyngedig ("**DCC**") or any statement about the future of DCC following completion of the Share Purchase Agreement (as defined below) or with respect to Glas or Glas Securities (as defined below) and certain of the assumptions in Chapter 9 under "Financial Projections of DCC" as stated therein (the "**Glas Information**"). To the best of the knowledge and belief of Glas (which has taken all reasonable care to ensure that such is the case), the Glas Information is in accordance with the facts and does not omit anything likely to affect the import of the Glas Information. Glas accepts no responsibility for any other information contained in this Information Memorandum and has not separately verified any such other information.*

*No representation, warranty or undertaking is made, and no responsibility is accepted, by DCC, the Guarantors, MBIA (or any other financial guarantor in respect of Class A Bonds), MBIA Insurance Corporation, Glas Securities, Glas, the Issuer Security Trustee, the Bond Trustee, the DCC Security Trustee, WPD Finance, WPDH, WPDL, HUH, HSU, the Liquidity Facility Providers, the Hedge Counterparties, the Authorised Loan Providers, the Finance Lessors, the Existing DCC Hedge Counterparty, the Cash Manager, the Dealers, the Class R Underwriters or the Co-Arrangers (each as defined below and, together, the "**Other Parties**") or any affiliate of any of them (other than the Issuer) as to the accuracy or completeness of any information contained in this Information Memorandum (other than, in respect of MBIA, the MBIA Information and, in respect of Glas, the Glas Information) or any other information supplied in relation to the Bonds or their distribution. None of the Other Parties (except MBIA in respect of the MBIA Information and Glas in respect of the Glas Information) has made any independent investigation or verification of the accuracy or completeness of any information contained in this Information Memorandum and none of them is responsible for any of the information contained in this Information Memorandum.*

The Issuer, MBIA (in relation to the MBIA Information only) and Glas (in relation to the Glas Information only) have each confirmed to the Dealers and the Class R Underwriters (as defined in Chapter 14: "Subscription and Sale") that this Information Memorandum (including, for this purpose, each relevant Pricing Supplement) is or, as the case may be, will be true, accurate and complete in all material respects and is not or, as the case may be, will not be misleading; that the opinions and intentions expressed herein are honestly held and based on reasonable assumptions; that there are no other facts in relation to the information contained or incorporated by reference in this Information Memorandum the omission of which would, in the context of the Programme or the issue of Bonds, make any statement herein or opinions or intentions expressed herein misleading in any material respect; and that all reasonable enquiries have been made to verify the foregoing. The Issuer has further confirmed to the Dealers that this Information Memorandum (together with, as the case may be, the relevant Pricing Supplement) contains or, as the case may be, will contain all such information as may be required by all applicable laws, rules and regulations.

No person has been authorised to give any information or to make any representation not contained in or not consistent with this Information Memorandum or any other document entered into in relation to the Programme or any information supplied by the Issuer, Glas or MBIA or such other information as is in the public domain and, if given or made, such information or representation should not be relied upon as having been authorised by the Issuer, the Other Parties or any of their respective affiliates.

Neither the delivery of this Information Memorandum or any Pricing Supplement nor the offering, sale or delivery of any Bond shall, in any circumstances, create any implication that the information contained in this Information Memorandum is true subsequent to the date hereof or the date upon which this Information Memorandum has been most recently amended or supplemented or that there has been no adverse change in the financial situation of the Issuer, DCC, any Guarantor (as defined below) or MBIA since the date hereof or, if later, the date upon which this Information Memorandum has been most recently amended or supplemented or that any other information supplied in connection with the Programme is correct at any time subsequent to the date on which it is supplied or, if different, the date indicated in the document containing the same.

*The distribution of this Information Memorandum and any Pricing Supplement and the offering, sale and delivery of Bonds in certain jurisdictions may be restricted by law. Persons into whose possession this Information Memorandum or any Pricing Supplement comes are required by the Issuer and the Other Parties to inform themselves about and to observe any such restrictions. The Bonds have not been and will not be registered under the United States 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. Accordingly, the Bonds may not be offered, sold or otherwise transferred except in a transaction outside the United States to persons that are not U.S. persons in accordance with Rule 903 or Rule 904 of Regulation S under the Securities Act. The Bonds may include Bonds that are in bearer form that are subject to U.S. tax law requirements. In addition, the Issuer has not authorised any offer of the Bonds to the public in the United Kingdom within the meaning of the Public Offers of Securities Regulations 1995, as amended (the ''**POS Regulations**''). Bonds may not lawfully be offered or sold to persons in the United Kingdom except in circumstances which do not result in an offer to the public in the United Kingdom within the meaning of the POS Regulations or otherwise in compliance with all applicable provisions of the POS Regulations. No invitation will be made to the public in the Cayman Islands to subscribe for the Bonds. For a description of certain restrictions on offers, sales and deliveries of Bonds and on the distribution of this Information Memorandum or any Pricing Supplement and other offering material relating to Bonds, see Chapter 14: ''Subscription and Sale''.*

Neither this Information Memorandum nor any Pricing Supplement constitutes an offer or an invitation to subscribe for or purchase any Bonds and should not be considered as a recommendation by the Issuer or the Other Parties or any of them that any recipient of this Information Memorandum or any Pricing Supplement should subscribe for or purchase any Bonds. Each recipient of this Information Memorandum or any Pricing Supplement shall be taken to have made its own investigation and appraisal of the condition (financial or otherwise) of the Issuer, DCC, each Guarantor and MBIA and must make its own determination of the suitability of any investment in the Bonds with particular reference to its own investment objectives and experience and any other factors which may be relevant to it in connection with such investment.

The Issuer and the Other Parties do not represent that this document may be lawfully distributed, or that any Bonds may be lawfully offered, in compliance with any applicable registration or other requirements in any jurisdiction, or pursuant to an exemption available thereunder, or assume any responsibility for facilitating any such distribution or offering. In particular, no action has been taken by the Issuer or the Other Parties (save for the approval of this document by the Luxembourg Stock Exchange) which would permit a public offering of any Bonds or distribution of this document or any Pricing Supplement in any jurisdiction where action for that purpose is required. Accordingly, no Bonds may be offered or sold, directly or indirectly, and neither this Information Memorandum, any Pricing Supplement 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, and the Dealers and the Class R Underwriters have represented that all offers and sales will be made by them on the same terms. Persons into whose possession this Information Memorandum or any Pricing Supplement or any Bonds come are required by the Issuer and the Other Parties to inform themselves about, and observe, any such restrictions. For a description of certain restrictions on offers and sales of the Bonds and distribution of this Information Memorandum or any Pricing Supplement, see Chapter 14: ''Subscription and Sale''.

*All references in this Information Memorandum to "sterling" and "£" refer to the lawful currency of the United Kingdom, to "U.S. dollars" and "$" refer to the lawful currency of the United States of America, to "French Francs" and "FF" refer to French Francs, a non-decimal sub-unit of the euro, and to "euro" and "€" refer to the lawful currency of member states of the European Community (the "**Member States**") that have adopted the euro as their lawful currency in accordance with the Treaty establishing the European Community, as amended by the Treaty on European Union and the Treaty of Amsterdam.*

In connection with the issue of any Sub-Class of Bonds, the person (if any) who is specified in the relevant Pricing Supplement as the stabilising manager may over-allot or effect transactions which stabilise or maintain the market price of such Bonds at a level which might not otherwise prevail. Such stabilising, if commenced, may be discontinued at any time. Such stabilising shall be in compliance with all applicable laws, regulations and rules.

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DOCUMENTS INCORPORATED BY REFERENCE

The following documents shall be deemed to be incorporated in, and to form part of, this Information Memorandum:

- the most recently published annual audited financial statements of the Issuer and DCC from time to time, and the semi-annual interim financial statements (whether audited or unaudited) of DCC published subsequently to such annual financial statements from time to time;
- the most recently published annual audited financial statements of MBIA and MBIA Insurance Corporation, and, in the case of MBIA Insurance Corporation, the quarterly interim financial statements (whether audited or unaudited) published subsequently to such annual financial statements, from time to time; and
- all supplements and addenda to this Information Memorandum circulated by the Issuer from time to time in accordance with its undertaking described below given by it in the Dealership Agreement (as defined in Chapter 14: ''*Subscription and Sale*'').

However, any statement contained herein, or in the documents deemed to be incorporated by reference herein, shall be deemed to be modified or superseded for the purpose of this Information Memorandum to the extent that a statement contained in any such subsequent document all or the relative portion of which is or is deemed to be incorporated by reference herein modifies or supersedes such earlier statement.

The Issuer will provide, free of charge, upon oral or written request, a copy of this Information Memorandum (or any document incorporated by reference in this Information Memorandum) at the specified offices of the Bond Trustee and the Luxembourg Listing Agent (as defined below) and (in the case of Bearer Bonds) at the offices of the Paying Agents and (in the case of Registered Bonds) at the offices of the Registrar and the Transfer Agents.

SUPPLEMENTARY INFORMATION MEMORANDUM

The Issuer has undertaken, in connection with the listing of the Bonds on the Luxembourg Stock Exchange, that, if there shall occur any adverse change in the business or financial position of the Issuer, DCC, the Guarantors (as defined below) or MBIA or any change in the information set out in Chapter 6 under ''*Terms and Conditions of the Bonds*'' that is material in the context of the issue of Bonds under the Programme, the Issuer will prepare or procure the preparation of an amendment or supplement to this Information Memorandum or, as the case may be, publish a new information memorandum for use in connection with any subsequent issue by the Issuer of Bonds to be listed on the Luxembourg Stock Exchange and will supply to each Dealer or Class R Underwriter such number of copies of the supplementary or new information memorandum as such Dealer or Class R Underwriter may reasonably request. The Issuer will also supply to the Luxembourg Stock Exchange such number of copies of the supplementary or new information memorandum as may be required by the Luxembourg Stock Exchange and will make copies available, free of charge, upon oral or written request, at the specified office of the Luxembourg Listing Agent.

CHAPTER 1

THE PROGRAMME

The following is a brief summary only and should be read in conjunction with the rest of this Information Memorandum and, in relation to any Bonds, in conjunction with the relevant Pricing Supplement and, to the extent applicable, the Conditions of the Bonds set out herein or therein.

Introduction and Use of Proceeds: An amount equal to the sterling equivalent of the gross proceeds of issue or, in the case of Class R Bonds, sale of each Series of Bonds will be advanced by the Issuer to DCC under the terms of an Intercompany Loan Agreement (see Chapter 4 under "*Intercompany Loan Agreements*" and "*Class R Bonds*").

Initial Programme Amounts: *Guaranteed Asset-Backed Bonds:* The maximum aggregate principal amount of Guaranteed Asset-Backed Bonds which may be outstanding under the Programme shall be £3,000,000,000 or the equivalent thereof in permitted currencies.

Asset-Backed Bonds: The maximum aggregate principal amount of Asset-Backed Bonds (including the Class R Bonds) which may be outstanding under the Programme shall be £3,000,000,000 or the equivalent thereof in permitted currencies.

Class R Bonds: The maximum aggregate principal amount of Class R Bonds which may be outstanding under the Programme shall be £200,000,000.

For the purpose of calculating the sterling (the "**Base Currency**") equivalent of the principal amount of Bonds outstanding under the Programme from time to time, the Base Currency equivalent of Bonds denominated in another currency shall be determined by the Agent Bank (as defined below) on the basis of the currency exchange rate under the relevant Hedging Agreement on the last preceding day on which commercial banks and foreign exchange markets were open for business in London.

Issue Dates: 10 May 2001, or such other date as the Co-Arrangers and the Issuer may agree, (the "**Initial Issue Date**") and thereafter on such dates (each an "**Issue Date**") as agreed between the Issuer and the Dealers.

Issuance in Series: Bonds issued on the same date will comprise a series (each, a "**Series**"). Each Series may comprise one or more non-fungible classes (each a "**Class**") or sub-classes (each a "**Sub-Class**"). The Bonds will be divided into five Classes, respectively, the "**Class A Bonds**, the "**Class B Bonds**", the "**Class R Bonds**", the "**Class C Bonds**" and the "**Class D Bonds**".

The Issuer may make further issues on identical terms to an existing Sub-Class save for the first payment of interest. Such further issue will be fungible with the earlier issue.

The specific terms of each Sub-Class of Bonds will be set out in the applicable Pricing Supplement.

Status and Ranking: The Bonds will constitute direct, secured and unconditional obligations of the Issuer. Each Sub-Class of Bonds will rank *pari passu* without preference or priority in point of security amongst all other Sub-Classes of Bonds.

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 Conditions (as defined below) and the trust deed (the "**Trust Deed**") to be entered into by the Issuer, the Bond Trustee and MBIA in connection with the Programme and

(b) in the case of the Class A Bonds only, from the relevant Financial Guarantor (as defined below) in certain circumstances in accordance with the relevant Bond Policy.

The Class A Bonds, Class B Bonds and Class R Bonds (each of whatever Sub-Class) will rank *pari passu* with respect to payments of interest. However, only the Class A Bonds will have the benefit of the relevant Bond Policy. All claims in respect of the Class A Bonds, Class B Bonds and Class R Bonds (each of whatever Sub-Class) will rank in priority to payments of interest due on all Sub-Classes of the Class C Bonds and Class D Bonds (other than any Subordinated Coupon Amounts), and the Class C Bonds (of whatever Sub-Class) will rank in priority to payments of interest due on all Sub-Classes of the Class D Bonds (other than any Subordinated Coupon Amounts).

The Class A Bonds, Class B Bonds and Class R Bonds (each of whatever Sub-Class) will rank *pari passu* with respect to repayment of principal. However, only Class A Bonds will have the benefit of the relevant Bond Policy. All claims in respect of the Class A Bonds, Class B Bonds and Class R Bonds (each of whatever Sub-Class) will rank in priority to repayments of principal due on all Sub-Classes of the Class C Bonds and Class D Bonds and the Class C Bonds (of whatever Sub-Class) will rank in priority to payments of principal due on all Sub-Classes of Class D Bonds.

Form of Bonds: Bonds will be issued in bearer and/or in registered form. Bonds issued in registered form will not be exchangeable for Bonds in bearer form.

Bearer Bonds: Each Sub-Class of Bonds issued in bearer form will initially be in the form of a Temporary Global Bond or a Permanent Global Bond (each, a "**Global Bond**") in each case as specified in the relevant Pricing Supplement. Each Global Bond will be deposited on or around the relevant issue date with a depositary or a common depositary for Euroclear Bank S.A./N.V., as operator of the Euroclear System ("**Euroclear**") and/or Clearstream Banking, société anonyme ("**Clearstream, Luxembourg**") and/or any other relevant clearing system. Each Temporary Global Bond will be exchangeable for a Permanent Global Bond or, if so specified in the relevant Pricing Supplement, for definitive Bonds in bearer form ("**Definitive Bonds**") with (if the Bonds bear interest) interest coupons ("**Coupons**") and (if applicable) talons for further Coupons ("**Talons**") attached. If the TEFRA D Rules are specified in the relevant Pricing Supplement as applicable, certification as to non-U.S. beneficial ownership will be a condition precedent to any exchange of an interest in a Temporary Global Bond or receipt of any payment of interest in respect of a Temporary Global Bond. A Permanent Global Bond will be exchanged for Definitive Bonds with (if the Bonds bear interest) Coupons and (if applicable) Talons attached in the circumstances specified in the Permanent Global Bond. See Chapter 6: "*The Bonds – Provisions Relating to the Bonds while in Global Form*".

Registered Bonds: For each Sub-Class of Bonds issued in registered form, the Issuer will deliver a global bond certificate (a "**Regulation S Global Registered Bond Certificate**") to a depositary or common depositary for Euroclear and/or Clearstream Luxembourg. Regulation S Global Registered Bond Certificates

will be exchangeable only for individual registered bond certificates ("**Regulation S Individual Registered Bond Certificates**") and only in the limited circumstances specified in the relevant Regulation S Global Registered Bond Certificate and as specified in the relevant Pricing Supplement.

All such Regulation S Individual Registered Bond Certificates will, if the principal thereof is repayable by instalments, have endorsed thereon a grid for recording the repayment of principal.

Currency: Bonds will be denominated in sterling, euro, U.S. dollars and/or other currency, as specified in the relevant Pricing Supplement.

Security: The Bonds will be secured pursuant to a deed of charge (the "**Issuer Deed of Charge**") (a) by first ranking security interests in favour of the Issuer Security Trustee over, *inter alia*, (i) the Issuer's interest in and to the DCC STID (as defined below), (ii) the Issuer's rights under each Issuer Transaction Document (as defined below) with certain exceptions, (iii) the Issuer's Accounts (as defined below) and (iv) certain investments to be made from time to time by, or on behalf of, the Issuer and (b) by a first floating charge in favour of the Issuer Security Trustee over all the assets and undertaking of the Issuer, in each case excluding all monies constituting the issued share capital of the Issuer not otherwise utilised by the Issuer from time to time and the corporate benefits fee of £1,000 payable by DCC to the Issuer (such fixed and floating security, together, the "**Issuer Security**"). The Issuer Security will be held by the Issuer Security Trustee on trust for the Issuer Secured Creditors (as defined below) under the terms of the Issuer Deed of Charge and subject to the terms of the Issuer STID (as defined below).

Intercreditor Arrangements: The Issuer Secured Creditors will each be party to the Issuer STID, pursuant to which they will agree that certain decisions in respect of the Issuer and the Issuer Security will be made by the Issuer Instructing Group (as defined below). Intercreditor arrangements will also be in place among the DCC Secured Creditors (as defined below). See Chapter 4 under "*Summary of Intercreditor Arrangements", "DCC STID" and "Issuer STID*".

Status of Bond Policies: Each financial guarantee insurance policy (each a "**Bond Policy**") issued in favour of the Bond Trustee in relation to each Sub-Class of Class A Bonds will be 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 will guarantee the timely payment of interest and principal (other than any accelerated or additional amounts or any Subordinated Coupon Amounts) on the relevant Sub-Class of Class A Bonds.

Counter-Indemnity: The Issuer will be 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 will be subrogated to the rights of the relevant Class A Bondholders against the Issuer in respect of any payments made under such Bond Policies. See Chapter 7: "*MBIA and the Bond Policies*" in respect of Class A Bonds issued on the Initial Issue Date.

Issue Price:	Bonds may be issued at any price, as specified in the relevant Pricing Supplement.
Maturities:	Bonds may be issued for any maturity (the ''**Expected Maturity Date**''), as specified in the relevant Pricing Supplement, but no Bonds will have a minimum maturity of less than three years from the relevant Issue Date.
Redemption:	Bonds will be redeemable at par or at such other amount detailed in a formula or otherwise as may be specified in the relevant Pricing Supplement. Bond Policies will not guarantee the payment of any amounts of principal in excess of the Principal Amount Outstanding (as defined in Condition 6 (i)), plus, in the case of Indexed Bonds, amounts in respect of indexation in respect of Class A Bonds.
Optional Redemption:	Upon giving not more than 60 nor less than 30 days' notice to the Bond Trustee, the Financial Guarantor(s) and the Bondholders (as defined below), the Issuer may (prior to the relevant Expected Maturity Date) redeem the Bonds in whole or in part (but on a *pro rata* basis only) on any Interest Payment Date (as defined in Condition 6(i), and, together with any interest payment date under any loan facilities made available to the Issuer, each an ''**Issuer Payment Date**''), provided that Floating Rate Bonds may not be redeemed before the date specified in the relevant Pricing Supplement, at the Redemption Amount (as defined in Condition 6(i)) plus accrued but unpaid interest. In respect of Fixed Rate Bonds, the Redemption Amount will be an amount equal to the higher of (i) their Principal Amount Outstanding and (ii) an amount calculated in accordance with the formula, as set out in Condition 8(b)(i). In respect of Floating Rate Bonds, the Redemption Amount will be the Principal Amount Outstanding, plus any premium for early redemption in certain years (as specified in the relevant Pricing Supplement), as set out in Condition 8(b)(ii). In respect of Indexed Bonds, the Redemption Amount will be the higher of (i) the Principal Amount Outstanding (plus an amount in respect of indexation) and (ii) an amount calculated in accordance with the formula as set out in Condition 8(b)(iii). In any such case, prior to giving any such notice, the Issuer must certify to the Bond Trustee that it will have the funds, not subject to any interest of any other person, required to redeem the Bonds as aforesaid. There are certain restrictions on the optional redemption of the Class C Bonds (see Condition 8(b)). Under the terms of the Bond Policies, the Financial Guarantors will not guarantee any of the amounts payable by the Issuer upon an optional redemption of the Bonds, and their obligations continue to be to pay the Insured Amounts (as defined below) as they fall due for payment on each Issuer Payment Date. The Financial Guarantors will not be obliged under any circumstances to accelerate payments under the Bond Policies. However, if they do so in their absolute discretion, following an acceleration of the Bonds only, they may do so in whole or in part and the amount payable will be the Principal Amount Outstanding (or, in the case of partial redemption, the pro rata amount that has become due and payable) of such Bonds, plus (i) in the case of Fixed Rate Bonds or Floating Rate Bonds, any accrued but unpaid interest (other than any Subordinated Coupon Amounts) and (ii) in the case of Indexed Bonds, an amount in respect of indexation and any accrued but unpaid interest (other than any Subordinated Coupon Amounts).

Redemption for Index Event, Taxation or Other Reasons:

Upon the occurrence of certain index events, the Issuer may redeem the Indexed Bonds at their Principal Amount Outstanding together with accrued but unpaid interest and amounts in respect of indexation. No single Sub-Class of Indexed Bonds may be redeemed in these circumstances unless all the other Sub-Classes of Indexed Bonds are also redeemed at the same time.

In addition, in the event of the Issuer becoming obliged to make any deduction or withholding from payments in respect of the Bonds (although the Issuer will not be obliged to pay any additional amounts in respect of such deduction or withholding) the Issuer may (a) use its reasonable endeavours to arrange for the substitution of another company in an alternative jurisdiction (subject to certain conditions as set out in Condition 8(c) of the Bonds) and, failing this, (b) redeem (subject to certain conditions as set out in Condition 8(c) of the Bonds) all but not some of the Bonds at their Principal Amount Outstanding (plus, in the case of Indexed Bonds, amounts in respect of indexation) together with accrued but unpaid interest. No single Class or Sub-Class of Bonds may be redeemed in these circumstances unless all the other Classes and Sub-Classes of Bonds are also redeemed in full at the same time.

In the event of DCC electing to prepay an advance (in whole or in part) under an Intercompany Loan Agreement following, *inter alia*, (i) DCC exercising its option to make such prepayment or (ii) DCC becoming obliged to make any deduction or withholding from payments under the relevant Intercompany Loan Agreement, the Issuer shall be obliged to redeem all or the relevant part of the corresponding Sub-Class of Bonds the proceeds of which were used by the Issuer to fund the making of the advance being prepaid.

The Financial Guarantors will not guarantee any of the amounts payable by the Issuer upon an early redemption and their obligations will continue to be to pay the Insured Amounts as they fall due for payment on each Issuer Payment Date. The Financial Guarantors will not be obliged under any circumstances to accelerate payments under the Bond Policies.

Redemption by Instalments:

The relevant Pricing Supplement may provide that a Sub-Class of Bonds may be redeemed in two or more instalments in such amounts and on such dates and on such other terms as may be specified therein.

Interest:

Bonds will, unless otherwise specified in the relevant Pricing Supplement, be interest bearing. Interest will accrue at a fixed or floating rate (plus, in the case of Indexed Bonds, amounts in respect of indexation) and will be payable in arrear, as specified in the relevant Pricing Supplement, or on such other basis and at such rate as may be so specified.

Fixed Rate Bonds:

Fixed Rate Bonds will bear interest at a fixed rate, and interest for such Sub-Class will be payable on such date(s) and at such rate(s) as agreed between the Issuer and the Dealers (as specified in the relevant Pricing Supplement).

Floating Rate Bonds: Floating Rate Bonds will bear interest at a rate set separately for each Sub-Class as may be specified in the relevant Pricing Supplement either on the basis of a reference rate appearing on an agreed screen page of a commercial quotation service or on the basis of quotations from reference banks or on such other basis as may be agreed between the Issuer and the Dealers and as adjusted for any applicable Margin (as defined in Condition 6(i)) (as specified in the relevant Pricing Supplement).

Indexed Bonds: Payments (whether in respect of principal or interest and whether at maturity or otherwise) in respect of Indexed Bonds (including Limited Indexed Bonds as defined in Condition 7(a)) may be calculated (with or without maximum and/or minimum limits on the amount of indexation) by reference to the UK Retail Price Index or such other index and/or formula as the Issuer and the Dealers may agree (as specified in the relevant Pricing Supplement).

Interest Payment Dates: Interest in respect of Fixed Rate Bonds will be payable annually in arrear, in respect of Floating Rate Bonds will be payable quarterly in arrear and in respect of Indexed Bonds will be payable semi-annually in arrear (in each case, or as otherwise specified in the relevant Pricing Supplement).

Hedging: On the Initial Issue Date, the Issuer will enter into interest rate and currency exchange swap agreements with the Initial Hedge Counterparties (as defined below). In most cases, the Issuer will make fixed-rate sterling advances to DCC (except advances of the proceeds of sale of Class R Bonds, the proceeds of drawings under its Authorised Loan Facilities or the proceeds of the issue of Indexed Bonds, which may be floating rate sterling advances or, as the case may be, fixed rate sterling advances subject to indexation under the relevant Intercompany Loan Agreement). (See Chapter 4 under "*Hedging Agreements*".)

Denominations: £1,000, £10,000 or £100,000, €1,000, €10,000 or €100,000 and $1,000, $10,000 or $100,000 or other denominations as specified in the relevant Pricing Supplement. The Bonds will be "longer term debt securities" issued in accordance with regulations under section 4 of the UK Banking Act 1987.

Authorised Loan Facilities: Subject to certain conditions being met, the Issuer and/or DCC will be permitted to incur indebtedness under authorised loan facilities (each an "**Authorised Loan Facility**") with an Authorised Lender (as defined below), providing revolving working capital and capital expenditure facilities. Authorised Loan Facilities available to DCC will be subject to a cap of £50,000,000 (as indexed) provided that the drawings by DCC from time to time under its Authorised Loan Facilities and the Overdraft Facility (as defined below) do not in the aggregate exceed £50,000,000 (as indexed). The Royal Bank of Scotland plc (as "**Initial Authorised Lender**") will make available an Authorised Loan Facility to each of the Issuer and DCC to be entered into on or before the Initial Issue Date. See Chapter 4 under "*Additional Resources Available*". Each Authorised Lender will be party to the Issuer STID or DCC STID, as the case may be, and may have voting rights thereunder. (See Chapter 4 under "*Issuer STID*" and "*DCC STID*".)

Liquidity Facilities: The Initial Liquidity Providers (as defined below) will make available to the Issuer a revolving 364-day credit facility for the purpose of meeting certain shortfalls in revenues: (i) for the Issuer to meet its obligations to pay interest on the first Series of

Class A Bonds, Class B Bonds, Class R Bonds and Class C Bonds (subject to certain limits in respect of the Class C Bonds) issued; (ii) for the Issuer or DCC, as the case may be, to make interest payments under any Authorised Loan Facilities entered into on or before the Initial Issue Date; or (iii) for DCC to make notional interest payments under the Finance Leases (see Chapter 4 under "*Intercompany Loan Agreements*"). Any further Series of Bonds, any other Authorised Loan Facilities and any further DCC Finance Leases (as defined below) will have the benefit of a separate liquidity facility from one or more banks (which may or may not be the Initial Liquidity Facility Providers, and, together with the Initial Liquidity Facility Providers, each a "**Liquidity Facility Provider**") for the purpose of meeting certain shortfalls in revenues available to the Issuer and DCC to meet their respective obligations to pay interest, including, *inter alia*, the obligations of the Issuer to pay interest on the Bonds of those Classes referred to above issued under that further Series.

Taxation: Payments in respect of Bonds or under the relevant Bond Policy will be made without withholding or deduction for, or on account of, any present or future taxes, duties, assessment 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 (see Chapter 13: "*Tax Considerations*"). 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 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.

Investor information: DCC will be required to produce an investors' report (the "**Investors' Report**") within 60 days of each 31 March and 30 September and within 45 days of each 30 June and 31 December (each a "**quarter-end**" and each period from but not including a quarter-end to and including the next quarter-end, a "**quarter**") starting with 30 September 2001. Such Investors' Report will include, *inter alia*: (i) the unaudited available net cashflows of DCC relative to debt service; (ii) details of the amounts applied in meeting certain of DCC's and the Issuer's obligations under the respective priorities of payments set out in Chapter 4 under "*DCC Cash Management*" and "*Issuer Cash Management*" on the immediately preceding quarter-end; (iii) movements in certain of DCC's Accounts during the immediately preceding quarter and closing balances; (iv) a summary of DCC's outstanding debt and principal payments and any indexation of balances made by DCC in the immediately preceding quarter; (v) the calculations of ICR and RAR (each as defined below) for the current financial year; (vi) the unaudited profit and loss statement, balance sheet and cashflow statement of DCC, for the immediately preceding quarter and, after 31 March 2002, a comparison with the same quarter in the previous year and for the year to date; and (vii) a general overview of DCC in respect of the immediately preceding quarter. Each such Investors' Report will be made available by DCC to the DCC Secured Creditors and Issuer Secured Creditors, including the Bondholders. DCC will also be required to make available unaudited interim accounts and audited annual accounts, within 90 days of 30 September and 180 days of

	31 March, respectively. DCC will also place certain additional information on Glas' website, as and when available. This will include, *inter alia*, the most recently published: (a) June Return – Summary Report setting out a summary of DCC's annual performance; (b) DCC's annual charges scheme, with details of tariffs; (c) summary of DCC's strategic business plan at each periodic review; (d) DCC's current Procurement Plan (as defined below); (e) DCC's annual drinking water quality report; (f) DCC's annual environment report; (g) DCC's annual conservation and access report; and (h) audited annual accounts and unaudited interim accounts of the Glas Group (as defined below) on a consolidated basis. (See Condition 3(h) in Chapter 6 under "*Terms and Conditions of the Bonds*".)
Governing Law:	The Bonds and all Issuer Transaction Documents and DCC Transaction Documents (each as defined below) will be governed by, and construed in accordance with, the laws of England and Wales.
Listing:	Application has been made to list the Bonds issued under the Programme on the Luxembourg Stock Exchange.
Terms and Conditions:	A Pricing Supplement will be prepared in respect of each Sub-Class of Bonds including further fungible issues of an existing Sub-Class. A copy of the Pricing Supplement will be delivered to the Luxembourg Stock Exchange on or before the Issue Date of such Bonds. The terms and conditions (the "**Conditions**") applicable to each such Sub-Class will be those set out in Chapter 6 under "*Terms and Conditions of the Bonds*", as amended, supplemented, varied or replaced by the relevant Pricing Supplement.
Clearing Systems:	Euroclear and/or Clearstream, Luxembourg and/or any other relevant clearing system as may be agreed between the Issuer and the relevant Dealers (as specified in the relevant Pricing Supplement).
Selling Restrictions:	For a description of certain restrictions on offers, sales and deliveries of Bonds and on the distribution of offering material in relation to the Bonds, see Chapter 14: "*Subscription and Sale*".

CHAPTER 2

THE PARTIES

Issuer: Dwr Cymru (Financing) Limited (the "**Issuer**") has been formed in order to raise funds to invest in providing long term debt financing to DCC in relation to its water and sewerage undertaking.

DCC: Dŵr Cymru Cyfyngedig ("**DCC**") is engaged in the provision of water and sewerage services under an appointment held under the UK Water Industry Act 1991 (the "**WIA**").

Holdings: Dŵr Cymru (Holdings) Limited ("**Holdings**") is the immediate holding company of the Issuer and DCC.

Guarantors: The following parties (each a "**Guarantor**") will each guarantee certain obligations of DCC in favour of the DCC Security Trustee (for itself and on behalf of the DCC Secured Creditors, as defined below): (i) Holdings; and (ii) until completion occurs under the Share Purchase Agreement (as defined below), HUH (as defined below)), and, from completion under the Share Purchase Agreement, each of Glas Securities and Glas (each as defined below). None of the Guarantors will guarantee the obligations of the Issuer under the Bonds.

Co-Arrangers: Salomon Brothers International Limited and The Royal Bank of Scotland plc are the co-arrangers of the Programme (the "**Co-Arrangers**").

Dealers: Salomon Brothers International Limited 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**") either generally in respect of the Programme (other than in respect of the Class R Bonds) or in relation to a particular Sub-Class, Class or Series of Bonds (other than in respect of the Class R Bonds).

Financial Guarantors (for Class A Bonds): MBIA Assurance S.A. ("**MBIA**"), under the terms of financial guarantee insurance policies which (subject to the satisfaction of certain conditions prior to the issue of the Class A Bonds on the Initial Issue Date) it may agree to issue in favour of the Bond Trustee in respect of such Class A Bonds (together with any other financial guarantee insurance policies issued by other Financial Guarantors (as defined below), the "**Bond Policies**"), will unconditionally and irrevocably guarantee the scheduled payment of interest and principal (but not any accelerated amounts or Subordinated Coupon Amounts) in respect of such Class A Bonds. (See Chapter 7 under "*MBIA Bond Policy*".) MBIA is under no obligation to issue Bond Policies. Subject to the approval of the Dealers and at least two of the Rating Agencies, the Issuer may arrange for such other financial institution (each a "**Financial Guarantor**"), in addition to MBIA, to issue Bond Policies in respect of further Series of Class A Bonds.

Class R Underwriters: Citibank, N.A. will act as initial underwriter (together with any other underwriter appointed from time to time by the Issuer, the "**Class R Underwriters**") in respect of the Class R Bonds.

Bond Trustee: Bankers Trustee Company Limited will act as trustee (the "**Bond Trustee**") for and on behalf of the holders of each Class of Bonds of each Series (each a "**Bondholder**").

Issuer Security Trustee: Bankers Trustee Company Limited will act as security trustee (the "**Issuer Security Trustee**") and will hold, and be entitled to enforce (for itself and on behalf of the Issuer Secured Creditors, as defined below), the Issuer Security (as defined below).

Paying Agents: Deutsche Bank AG London will act as issue agent and principal paying agent (the "**Principal Paying Agent**") and Deutsche Bank Luxembourg S.A. (the "**Luxembourg Paying Agent**" and, together with the Principal Paying Agent, the "**Paying Agents**") will provide certain paying agency services to the Issuer in respect of Bearer Bonds.

Registrar: Deutsche Bank Luxembourg S.A. will act as registrar (the "**Registrar**") and will provide certain registrar services to the Issuer in respect of Registered Bonds.

Transfer Agents: Deutsche Bank AG London will act as transfer agent (the "**Principal Transfer Agent**" and Deutsche Bank Luxembourg S.A. (the "**Luxembourg Transfer Agent**", together with the Principal Transfer Agent, the "**Transfer Agents**"), will provide certain transfer agency services to the Issuer in respect of Registered Bonds.

DCC Security Trustee: Bankers Trustee Company Limited will act as security trustee (the "**DCC Security Trustee**") and will hold, and be entitled to enforce (for itself and on behalf of the DCC Secured Creditors (as defined below)), the DCC Security and the Guarantor Security (each as defined below).

Cash Manager: DCC will pursuant to the terms of the Master Framework Agreement (as defined below) be appointed by the Issuer to act as cash manager (the "**Cash Manager**") in respect of monies credited from time to time to the Issuer Accounts (as defined below).

Standstill Cash Manager: The Royal Bank of Scotland plc will, pursuant to the terms of the DCC STID, be appointed to act as cash manager (the "**Standstill Cash Manager**") in respect of monies credited from time to time to the Debt Service Payment Account (as defined below).

Account Bank: National Westminster Bank Plc, or any person for the time being acting as Account Bank (pursuant to the DCC Account Bank Agreement and the Issuer Account Bank Agreement, each as defined below) (each an "**Account Bank**") will hold the DCC Accounts (as defined below) and Issuer Accounts and will establish the Overdraft Facility (as defined below) in favour of DCC.

Agent Bank: Deutsche Bank AG London will act as agent bank (the "**Agent Bank**") under the Paying Agency Agreement.

Luxembourg Listing Agent: BNP Paribas Luxembourg will be the listing agent in respect of the Bonds in Luxembourg.

Finance Lessors: Each of Abbey National March Leasing (1) Limited and Lloyds Plant Leasing Limited (together the "**Finance Lessors**" and, together with any finance lessors under DCC Finance Leases (as defined below), the "**DCC Finance Lessors**"), who lease plant, machinery and equipment to DCC under the terms of various finance leases (together, the "**Finance Leases**").

Existing DCC Hedge Counterparty: Gen Re Securities Limited (the "**Existing DCC Hedge Counterparty**") pursuant to an interest rate hedging agreement dated 16 March 1994 with DCC pursuant to which DCC has hedged its interest rate exposure under the Finance Lease with Abbey National March Leasing (1) Limited (the "**Abbey National Finance Lease**").

Liquidity Facility Providers: The Royal Bank of Scotland plc and Lloyds TSB Bank plc (the "**Initial Liquidity Facility Providers**") have agreed to provide to the Issuer a 364-day revolving credit facility for the purpose of meeting certain shortfalls in revenues available to the Issuer and DCC.

Hedge Counterparties: Citibank, N.A. and The Royal Bank of Scotland plc (the "**Initial Hedge Counterparties**") have entered into, or agreed to enter into, interest rate and currency exchange swap agreements with DCC prior to the Initial Issue Date, which will either be cancelled or novated to the Issuer on the Initial Issue Date in consideration for the Issuer entering into the Initial Intercompany Loan Agreement. The Issuer will be required to hedge its exposure in relation to any further Series of Bonds or other indebtedness for borrowed money in accordance with the Issuer's hedging strategy with hedge counterparties (which may or may not be the Initial Hedge Counterparties, each a "**Hedge Counterparty**") pursuant to interest rate and currency exchange swap agreements (each, together with such agreements entered into with the Initial Hedge Counterparties, respectively, an "**Interest Rate Hedging Agreement**" and a "**Currency Hedging Agreement**" and, together, the "**Hedging Agreements**"). For further details of the hedging strategy, see Chapter 4 under "*Hedging Agreements – Hedging Strategy*".

Authorised Lenders: The Royal Bank of Scotland plc, as initial authorised lender (the "**Initial Authorised Lender**") in respect of the revolving working capital and capital expenditure credit facilities provided to each of the Issuer and DCC on or before the Initial Issue Date and certain other banks or financial institutions (each an "**Authorised Lender**") which agree to provide revolving credit facilities to the Issuer and/or DCC. (See Chapter 4 under "*Additional Resources Available – Authorised Loan Facilities*".)

Contractors: DCC will, pursuant to its initial outsourcing plan, outsource the major components of operating and maintaining its water and sewerage undertaking and servicing its customers to qualified third parties ("**Contractors**"). (See Chapter 12 under "*Procurement and Outsourcing*" for a description of the outsourcing plan and the qualifications of Contractors.)

Glas: Glas Cymru Cyfyngedig ("**Glas**"), a private company limited by guarantee, the holding company in the Glas Group.

Glas Securities: Glas Cymru (Securities) Cyfyngedig ("**Glas Securities**"), a private company limited by shares which is a wholly owned subsidiary of Glas, has agreed, pursuant to the agreement dated 5 February 2001 between HUH, WPDH (each as defined below), Glas and Glas Securities (the "**Share Purchase Agreement**"), as amended, to acquire from HUH the Financing Group by acquiring all of the issued share capital of Holdings on, or as soon as reasonably practicable following, the Initial Issue Date.

Financing Group: Holdings, the Issuer and DCC (and its subsidiary Welsh Water Utilities Finance PLC ("**WWUF**")).

Glas Group: Glas, Glas Securities and (from completion under the Share Purchase Agreement) the Financing Group.

HUH: Hyder Utilities (Holdings) Limited ("**HUH**"), the current holding company of Holdings.

HSU: Hyder Securities (Utilities) Limited ("**HSU**").

WPD Finance: WPD Finance Limited ("**WPD Finance**"), a subsidiary of WPDH, which has entered into a contract for differences (the "**CfD**"), dated as of 14 March 2001, as amended and restated on 3 April

2001, with DCC under which DCC will hedge approximately 58 per cent. of DCC's operation and maintenance costs and customer service costs, and IT costs relating thereto, from 1 April 2001 to 31 March 2005. (See Chapter 12: "*Procurement and Outsourcing*".)

WPDH: WPD Holdings UK ("**WPDH**"), an unlimited company which guarantees the obligations of WPD Finance under the CfD pursuant to a guarantee dated as of 14 March 2001 and guarantees the obligations of HUH under the Share Purchase Agreement.

CHAPTER 3

HISTORY AND BACKGROUND

On 15 September 2000, WPD Limited ("**WPDL**") announced that its offer to acquire all the issued share capital of Hyder plc (since re-registered as Hyder Limited and referred to as "**Hyder**") had become unconditional. DCC and the other members of the Hyder group of companies (which included at that date, *inter alios*, Hyder, HUH, DCC, WWUF and South Wales Electricity plc (collectively, the "**Hyder Group**")) were acquired by WPDL through the acquisition of the shares of Hyder.

The existing debt structure of the Hyder Group at the time of acquisition included: (i) £675,000,000 fixed rate bonds issued by Hyder (the "**Hyder Sterling Bonds**"); (ii) £200,000,000 fixed rate bonds issued by WWUF (the "**WWUF Sterling Bonds**" and, together with the Hyder Sterling Bonds, the "**Sterling Bonds**"); and (iii) US$1,025,000,000 fixed rate bonds issued by Hyder ("**Hyder U.S. Dollar Bonds**"). Prior to WPDL's completion of the acquisition of the Hyder Group and following its initial cash offer in respect of such acquisition, WPDL offered to purchase or, at WPDL's discretion, to procure the purchase of the Sterling Bonds on the terms set out in a notice of terms of tender offer dated 8 August 2000 (the "**Sterling Tender Offer**").

On 19 December 2000, DCC, Hyder, WPDL and Citibank, N.A. and The Royal Bank of Scotland plc (the "**Facility Banks**") entered into a term facility agreement (the "**Bridge Facility Agreement**") pursuant to which the Facility Banks provided a term loan facility of up to £1,400,000,000 to DCC for the purposes of refinancing certain existing indebtedness of the Hyder Group, including, *inter alia*, the Sterling Bonds and intercompany loans made by Hyder to DCC.

On 17 January 2001, DCC borrowed £641,000,000 under the Bridge Facility Agreement which was wholly applied towards funding the repurchase by Hyder and WWUF of the Sterling Bonds tendered under the Sterling Tender Offer. The funds were transferred from DCC to Hyder by means of a repurchase for £428,727,955 of 166,173,626 of DCC's ordinary shares from HUH, and an interest free loan from HUH to Hyder. The whole of the balance of the £641,000,000 was used to repay loans from WWUF to DCC, thereby enabling WWUF to redeem the WWUF Sterling Bonds.

The Issuer was incorporated as a Cayman Islands registered exempted company with limited liability on 15 February 2001 and became a wholly owned subsidiary of Holdings on 16 March 2001 (see Chapter 9 under the "*The Issuer*").

On 7 March 2001, DCC borrowed a further £208,394,520 under the Bridge Facility Agreement to repay in full amounts owing, accrued interest and early repayment penalties under the project finance facilities provided by the European Investment Bank.

On 16 March 2001, DCC borrowed a further £300,000,000 under the Bridge Facility Agreement, the proceeds of which were applied, *inter alia*, by DCC to repay to Hyder amounts outstanding under certain intercompany loan agreements. Hyder used the funds from repayment of such intercompany loan agreements for partial consideration for the exchange by WPDH of the Hyder U.S. Dollar Bonds. Following such advance, Holdings granted a charge over the shares in DCC on 23 March 2001 in favour of the Facility Banks, to secure the obligations of DCC to the Facility Banks under the Bridge Facility Agreement. The Facility Banks have agreed to release the charge when the Facility Banks are satisfied that all secured obligations have been or will be unconditionally and irrevocably paid and discharged.

On 20 March 2001, Holdings issued 30,000 redeemable preferred ordinary shares with a nominal value of £1 each to Glas Securities. Holdings has used the proceeds of such issue to subscribe for 30,000 ordinary shares of £1 each in the Issuer.

On 22 March 2001, HSU transferred all the 200,000,000 7 per cent. issued preference shares owned by it in DCC to Holdings and on the same date HUH transferred all the 109,876,374 issued ordinary shares of £1 each owned by it in DCC to Holdings. The consideration for these transfers was approximately £450,000,000, such sum to be adjusted for capital expenditure and working capital movements and to be left outstanding on intercompany loan accounts. These intercompany loan accounts will be settled with a drawing under a loan to be made available to Holdings by DCC which will be repayable in full (subject to extension by agreement of the parties) on the later to occur of: (i) 31 March 2035 and (ii) the date which is two years and one day after the final maturity date of the longest dated Bonds. Interest on such loan is payable semi-annually at a rate of 12 per cent. per annum, but payment of such interest may be deferred (see Chapter 10 under "*Holdings/DCC Loan Agreement*").

On 30 April 2001, DCC borrowed a further £75,000,000 under the Bridge Facility Agreement, the proceeds of which were applied, together with other monies, by DCC to repay in full amounts owing and accrued interest under the finance lease provided by Capital Bank Leasing 3 Limited.

Pursuant to the Share Purchase Agreement, HUH shall on, or as soon as reasonably practicable following, the Initial Issue Date, transfer its ordinary shares in Holdings to Glas Securities (see Chapter 10 under "*Share Purchase Agreement*").

All drawings under the Bridge Facility Agreement will be repaid from the proceeds of the first Series of Bonds which will be on-lent by the Issuer to DCC under the Initial Intercompany Loan Agreement (see Chapter 4 under "*Intercompany Loan Agreements*").

CHAPTER 4

FINANCING STRUCTURE

THE FINANCING GROUP

The Financing Group consists of Holdings and its two direct wholly-owned subsidiaries (DCC and the Issuer) and one wholly-owned subsidiary of DCC (which will become a dormant company). See further Chapter 9 under "*The Financing Group*". The sole purpose for the creation of the Financing Group is to facilitate the refinancing and future financing of the operating and capital requirements of DCC through, *inter alia*, the issuance of Bonds and other financial indebtedness, from time to time, raised by the Issuer. DCC will be funded through loans made by the Issuer pursuant to Intercompany Loan Agreements as described below and through certain other available resources (see "*Additional Resources Available*" below).

FIGURE 1 – OWNERSHIP STRUCTURE

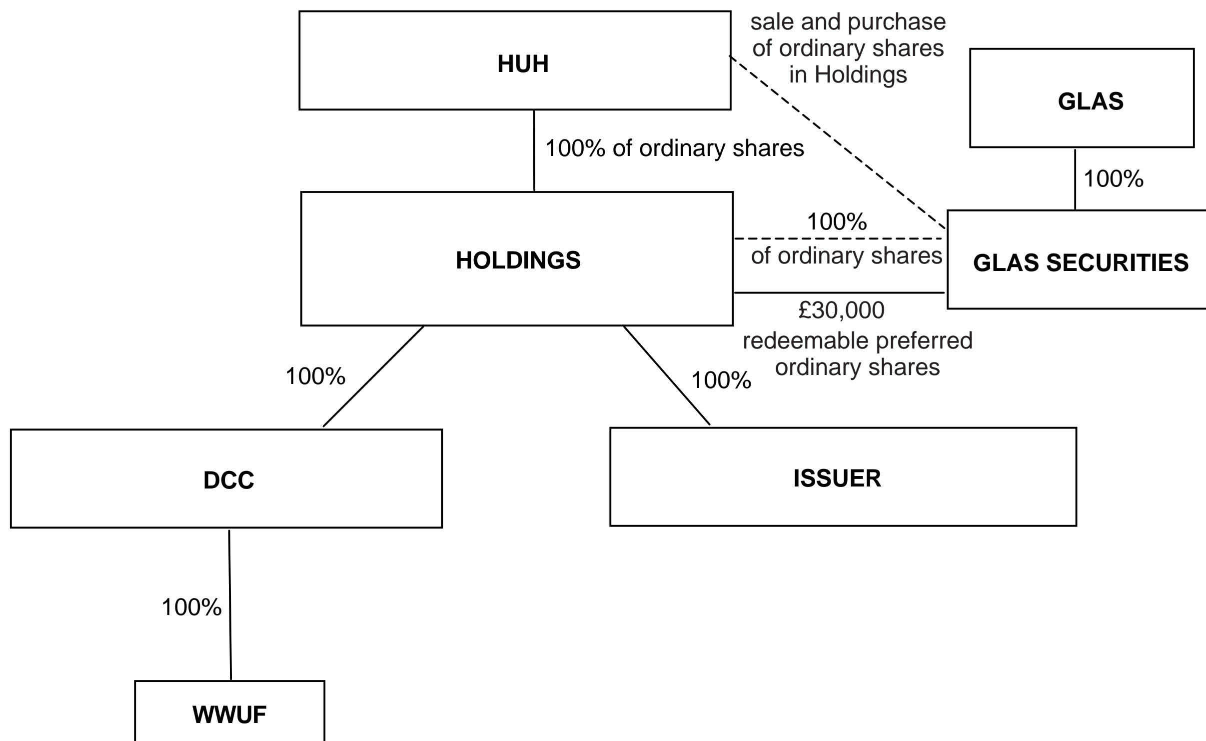


Figure 1 illustrates the ownership structure of the Financing Group:

- Each of DCC and the Issuer is a wholly-owned subsidiary of Holdings.
- 30,000 redeemable preferred ordinary shares of £1 each issued by Holdings are currently held by Glas Securities.
- All of the 1,000 issued ordinary shares of £1 each issued by Holdings is currently held by HUH.
- Holdings has agreed to guarantee DCC's obligations to the DCC Secured Creditors, to charge its interest in the ordinary and preference shares of DCC and the ordinary shares of the Issuer, to assign the benefit of its rights under the Holdings/DCC Loan Agreement and to grant first ranking fixed and floating charges over its assets and undertaking in favour of the DCC Security Trustee as security for its guarantee obligations (see "*Guarantor Security*" below).
- HUH has agreed to guarantee DCC's obligations to the DCC Secured Creditors, to charge its interest in the shares of Holdings and to grant a floating charge over its assets and undertaking in favour of the DCC Security Trustee as security for its guarantee obligations (until completion under the Share Purchase Agreement). The floating charge to be granted by HUH will become enforceable only upon presentation of a petition for the administration of HUH and not otherwise. (See "*Guarantor Security*" below and Chapter 10 under "*Share Purchase Agreement*".)
- HUH has agreed to sell all its shares in Holdings to Glas Securities on, or as soon as reasonably practicable following, the Initial Issue Date (see Chapter 10 under "*Share Purchase Agreement*").
- Glas Securities has agreed to guarantee DCC's obligations to the DCC Secured Creditors, to charge its interest in the ordinary shares it is to acquire in Holdings and the existing redeemable preferred ordinary shares it holds in Holdings, to assign the benefit of its rights under the Share Purchase Agreement and to grant first ranking fixed and floating charges over its assets and undertaking in favour of the DCC Security Trustee as security for its guarantee obligations (see "*Guarantor Security*" below).
- Glas has agreed to guarantee DCC's obligations to the DCC Secured Creditors, to charge its interest in the shares of Glas Securities and to grant first ranking fixed and floating charges over its assets and undertaking in favour of the DCC Security Trustee as security for its guarantee obligations (see "*Guarantor Security*" below).

FIGURE 2 – PROGRAMME STRUCTURE

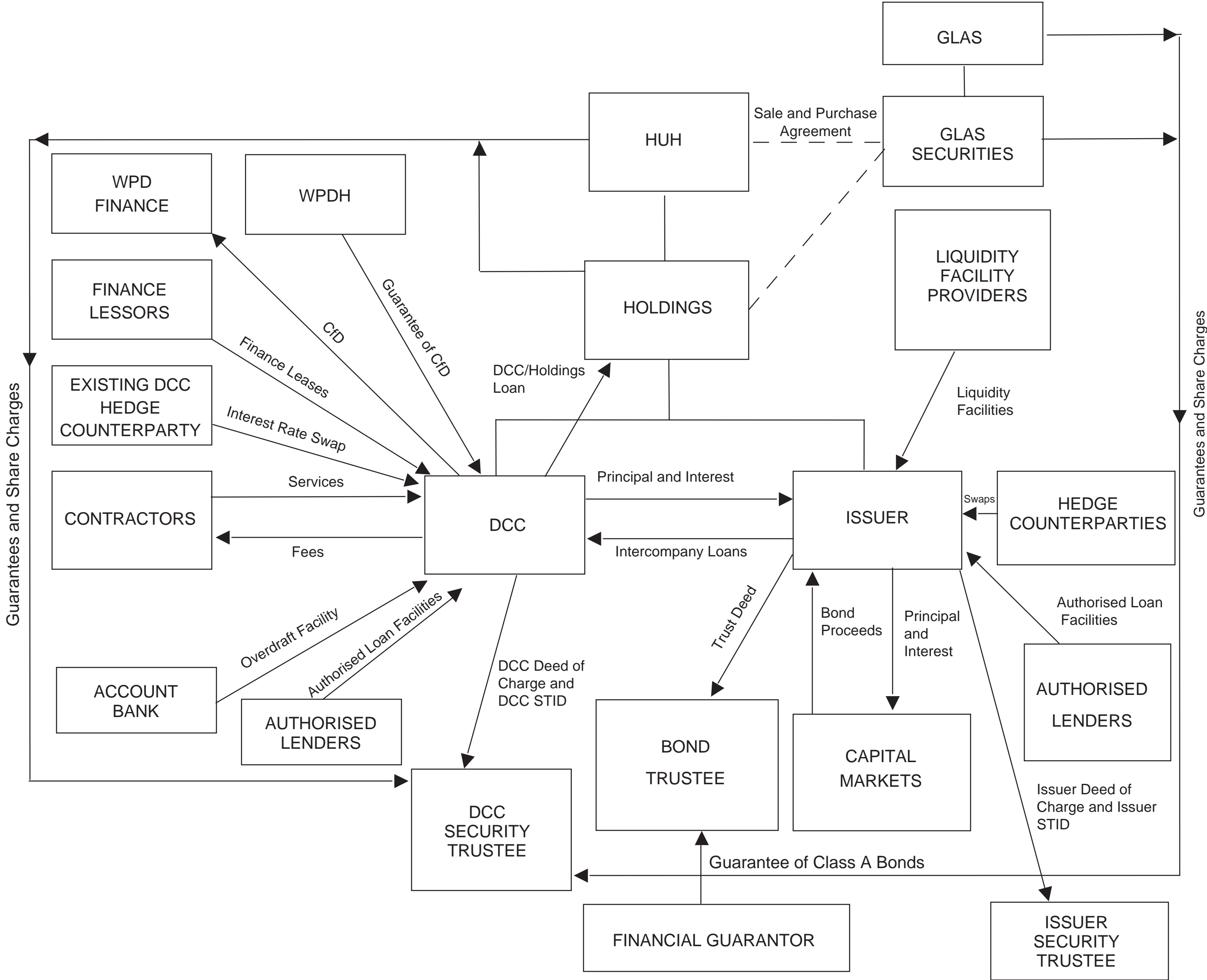


Figure 2 provides an overview of the Programme, as follows:

- The Issuer will issue Class A Bonds (as to which scheduled principal and interest will be guaranteed by MBIA or another Financial Guarantor), Class B Bonds, Class R Bonds, Class C Bonds and Class D Bonds.
- The Issuer will on-lend an amount equal to the equivalent in sterling of the gross proceeds of the issue of each Series of Bonds (other than the Class R Bonds) to DCC under the terms of an Intercompany Loan Agreement. There will be a separate Intercompany Loan Agreement for each Series and separate advances under each Intercompany Loan Agreement in respect of: (i) each different Sub-Class of Bonds issued in such Series; and (ii) additional liquidity provided under Liquidity Facility Agreements in respect of the Bonds of the relevant Series. There will also be a separate Intercompany Loan Agreement between DCC and the Issuer for the working capital and/or capital expenditure facilities provided to DCC via the Issuer through Authorised Loan Facilities (other than the Authorised Loan Facility entered into by the Issuer on the Initial Issue Date). The amount of each such advance will reflect the corresponding amount of borrowing by the Issuer under the Bonds, the relevant Authorised Loan Facility or the relevant Liquidity Facility, as the case may be (see "*Intercompany Loan Agreements*" below).
- The Issuer will use the proceeds of the issue of the Class R Bonds issued on the Initial Issue Date immediately to repurchase (but not cancel) such Class R Bonds, which it may then at any time thereafter (up to 31 March 2006) sell to the Class R Underwriters in accordance with the terms and conditions of the Class R Underwriting Agreement (see "*Class R Bonds*" below). The Issuer will use the proceeds of such sale or the proceeds of advances under the relevant Authorised Loan Facility to make R Advances (as defined below) to DCC under the Initial Intercompany Loan Agreement. (See "*Intercompany Loan Agreements*" below.)
- DCC will use the proceeds of each R Advance under the Initial Intercompany Loan Agreement (as defined below) towards its operation and maintenance costs, working capital and capital expenditure and will use the proceeds of each Term Advance (as defined below) thereunder for its corporate purposes, including the making of a loan of up to £459 million to Holdings (see "*Intercompany Loan Agreements*" below and Chapter 10 under "*Holdings/DCC Loan Agreement*") and the repayment of the monies advanced under the Bridge Facility Agreement (see Figure 3 below).
- The Issuer's obligations to pay principal and interest on, *inter alia*, the Bonds are intended to be met primarily from the payments of principal and interest received from DCC under each Intercompany Loan Agreement. (See "*Intercompany Loan Agreements*" and "*Additional Resources Available*" below.)
- The Issuer will hedge certain of its interest and/or currency exposures under the Bonds with the Hedge Counterparties in accordance with the agreed hedging strategy (see "*Hedging Agreements*" below).
- The Issuer may draw under the relevant Liquidity Facility provided in respect of any Series to fund liquidity advances to DCC to meet any shortfall in the amounts available to DCC to meet interest payments, *inter alia*, on any advances under any Term Advance (other than Tranche D and subject to certain limits in respect of any Advances made with the proceeds of Class C bonds) and on any R Advances of the corresponding Intercompany Loan Agreement for that Series, which in turn will meet, to the extent available, any shortfall which would otherwise have arisen under the Class A Bonds, Class B Bonds, Class R Bonds and Class C Bonds (subject to certain limits in respect of the Class C Bonds) of such Series. (See "*Liquidity Facilities*" below.)
- Pursuant to the initial outsourcing plan, DCC has outsourced to the Contractors the majority of its operation, maintenance and customer servicing functions. Certain information technology ("**IT**") services will be provided by Logica Services Limited ("**Logica**"). (See Chapter 12 under "*Initial Outsourcing*".)
- DCC has the benefit of the CfD under which WPD Finance is required to make annual difference payments to DCC to the extent that DCC's operation and maintenance costs, customer service costs, and IT costs relating thereto (excluding costs of IT services provided pursuant to the DCC ITA, as defined below) exceed a specified fixed amount (as described in Chapter 12 under "*Contract for Differences*") while DCC is required to make

annual difference payments to WPD Finance to the extent that these costs are below the specified fixed amount. WPDH has guaranteed the payment obligations (including any indemnity obligations) of WPD Finance under the CfD. However, it is expected that, on a net basis, an annual difference amount will be payable by DCC to WPD Finance. (See Chapter 12 under "*Contract for Differences*".)

- DCC may enter into Authorised Loan Facilities directly with Authorised Lenders in respect of its further working capital and/or capital expenditure requirements. (See "*Additional Resources Available*" below.)
- The Finance Lessors currently provide, and will continue to provide, financing of equipment to DCC. The Existing DCC Hedge Counterparty currently hedges, and will continue to hedge, DCC's interest rate exposure under the Abbey National Finance Lease. (See "*Additional Resources Available*" below.) DCC may enter into further DCC Finance Leases with DCC Finance Lessors (which may or may not be the existing Finance Lessors).
- DCC will use its revenue flows to meet its operating costs, capital expenditure and obligations to the DCC Secured Creditors, including the Issuer, and other third party creditors. (See Figure 4 below.)
- DCC's obligations to the DCC Secured Creditors will be secured, to the extent permitted by the WIA and its instrument of appointment under the WIA (the "**Licence**"), and requirements thereunder, by the DCC Deed of Charge. (See "*DCC Deed of Charge*" below.)
- The obligations of DCC to the DCC Secured Creditors will be guaranteed by the Guarantors. The guarantee obligations of each of HUH (until completion under the Share Purchase Agreement), Holdings and (subject to completion under the Share Purchase Agreement) each of Glas Securities and Glas will be secured by the Guarantor Security. (See "*Guarantor Security*" below.)
- The Issuer's obligations to the Issuer Secured Creditors under, *inter alia*, the Bonds, the Trust Deed, each Liquidity Facility Agreement, each Hedging Agreement, each I&I Agreement, the Paying Agency Agreement, the Master Framework Agreement, the Issuer STID and any Authorised Loan Facilities made available to the Issuer will be secured by the Issuer Deed of Charge and subject to the Issuer STID. (See "*Issuer Deed of Charge*" and "*Issuer STID*" below and Chapter 6 under "*Terms and Conditions of the Bonds*".)

FIGURE 3 – CASHFLOWS ON INITIAL ISSUE DATE

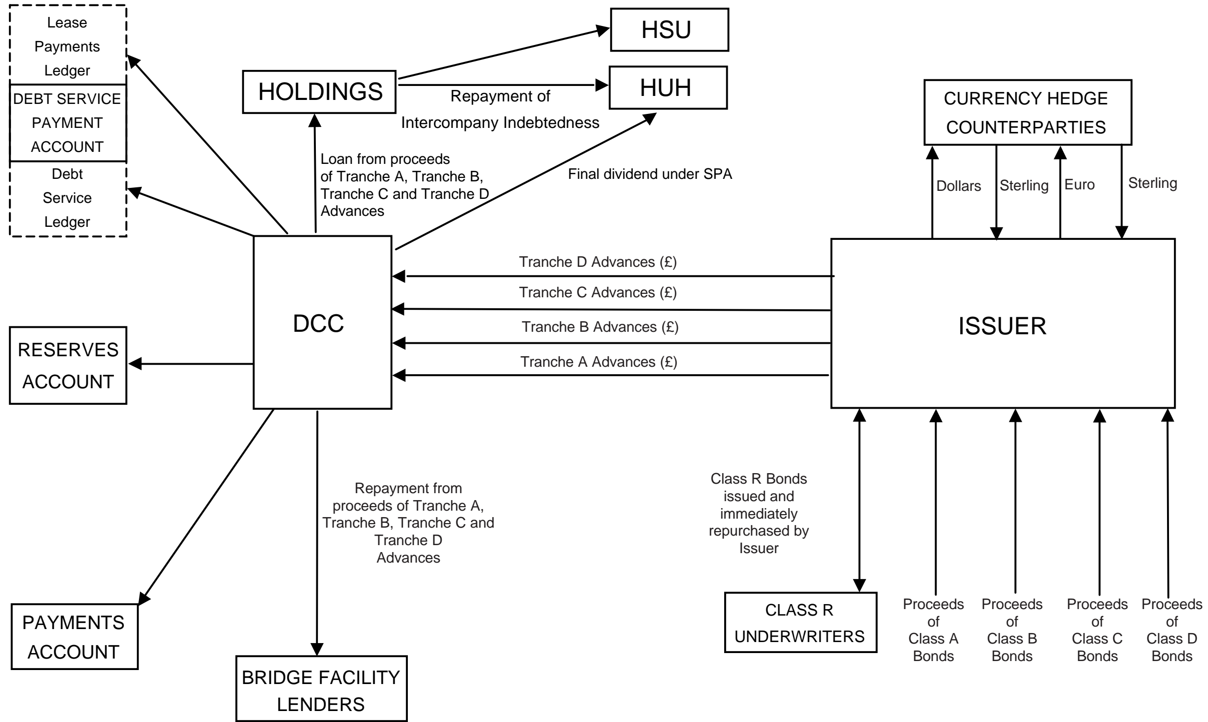
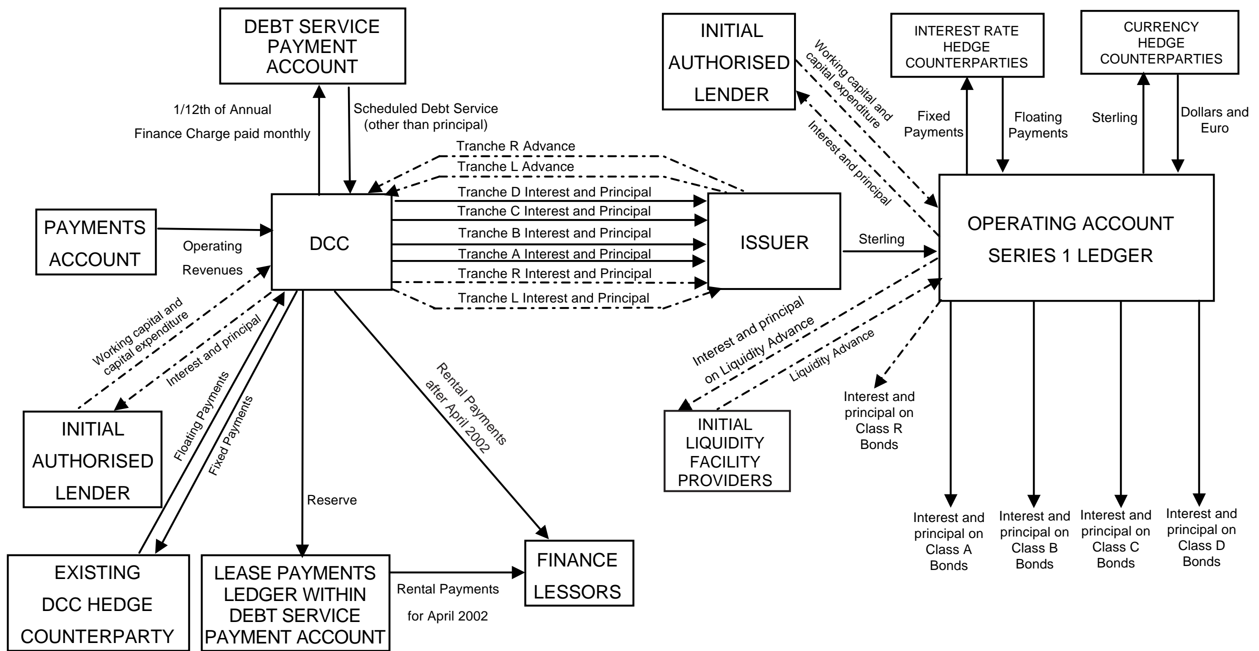


FIGURE 4 – TRANSACTION CASHFLOWS FOR INITIAL SERIES



SUMMARY OF INTERCREDITOR ARRANGEMENTS

This section is intended to provide a brief summary of the Intercreditor Arrangements. The detailed provisions of the DCC STID and the Issuer STID are set out in more detail under "DCC STID" and "Issuer STID" below. The meaning of certain defined terms which are used in this section are set out under "Intercreditor Definitions" below. In order to simplify this summary of the Intercreditor Arrangements, throughout this section it is assumed that the Qualifying Debt Representative for the Class A Bonds is a Financial Guarantor. If there is an FG Event of Default, then the Qualifying Debt Representative for the Class A Bonds will be the Bond Trustee and the Intercreditor Arrangements will then apply to the Class A Bonds as they do to the Class B Bonds and Class R Bonds.

Overview of the Intercreditor Arrangements

The intercreditor arrangements in respect of the Issuer and DCC (the "**Intercreditor Arrangements**") are contained in two security trust and intercreditor deeds (respectively, the "**Issuer STID**" and the "**DCC STID**"). The Intercreditor Arrangements bind the DCC Secured Creditors and the Issuer Secured Creditors (together the "**Intercreditor Parties**"). Any Additional Beneficiary of the DCC Security and the Guarantor Security will be required to accede to the DCC STID and any Additional Beneficiary of the Issuer Security will be required to accede to the Issuer STID (as in each case will certain other creditors of DCC and the Issuer). The Local Authority Loans (as defined below) are not subject to the Intercreditor Arrangements.

The purpose of the Intercreditor Arrangements is to regulate, *inter alia:* (i) claims of the Intercreditor Parties; (ii) the exercise and enforcement of rights by those parties; (iii) the rights of such parties to instruct the Issuer Security Trustee and the DCC Security Trustee (each a "**Security Trustee**" and together the "**Security Trustees**"); (iv) the rights of such parties during a Default Situation; (v) the entrenched rights and reserved matters of each Intercreditor Party; and (vi) the giving of consents and waivers and the making of amendments by the Intercreditor Parties.

The Intercreditor Arrangements provide for the ranking in point of payment of the Intercreditor Parties: (i) prior to the occurrence of a Standstill (see "*DCC Cash Management – Debt Service Payment Account*" and the Issuer Pre-Enforcement Payments Priorities set out in "*Issuer Cash Management*" below); (ii) during a Standstill (see "*DCC Cash Management – DCC Standstill Priority*" below and the paragraph preceding that heading); and (iii) following an acceleration under either of the DCC STID or the Issuer STID (see DCC Post-Enforcement Payments Priorities set out under "*DCC Cash Management*" and Issuer Post-Enforcement Payments Priorities set out under "*Issuer Cash Management*" below).

The Intercreditor Parties (other than, with respect to certain permitted voluntary terminations, the Finance Lessors and the Existing DCC Hedge Counterparty in certain limited circumstances) do not have the right independently to accelerate their claims or take other enforcement action. The DCC Security Trustee will be instructed by the Beneficiary Instructing Group. The Issuer has assigned its rights under the DCC STID to the Issuer Security Trustee for itself and on behalf of the Issuer Secured Creditors under the Issuer Deed of Charge. The Issuer Security Trustee will be instructed by the Issuer Instructing Group.

The Intercreditor Arrangements provide a regime for instructing the Issuer Security Trustee at the Issuer level and a regime for instructing the DCC Security Trustee at the DCC level. At the DCC level the Issuer Security Trustee votes on behalf of the Issuer proportionately according to the votes received at the Issuer level. In each case, the relevant Security Trustee will not be liable to any person in relation to actions taken or not taken by it and will not be obliged to take action unless indemnified and/or secured to its satisfaction.

The underlying principle of the Intercreditor Arrangements is, prior to a Default Situation, that the Class A Bonds and the Authorised Loan Facilities and, after a Default Situation, that the Class A Bonds, Class B Bonds, Class R Bonds and Authorised Loan Facilities at the Issuer level and the DCC Finance Leases, Authorised Loan Facilities and Intercompany Loan Agreements at the DCC level shall have a potential vote (or be able to instruct) in respect of the outstanding principal amount of the relevant debt. Such votes may only be exercised through the relevant Qualifying Debt Representative. This basic principle will not apply where a vote on an Intercreditor Issue involves a Basic Terms Modification (as defined in the Conditions), in which case the usual provisions for meetings in respect of the Bonds shall apply (see Condition 15(b)(i) in Chapter 6 under "*Terms and Conditions of the Bonds*"). In the absence of a Default Situation, a Qualifying Debt Representative (other than the Bond Trustee) may only vote or

instruct if it has provided an Appropriate Indemnity. In a Default Situation there is no requirement on any DCC Secured Creditor or Issuer Secured Creditor to provide an Appropriate Indemnity to the relevant Security Trustee in order to exercise a vote or give instructions.

In order to facilitate timely decision-making prior to a Default Situation of the Bonds, only the Issuer Qualifying Debt Representative of the Class A Bonds will instruct the Issuer Security Trustee.

However, at any time during a Default Situation, the Qualifying Debt Representative of the Class B Bonds and Class R Bonds in addition to the Qualifying Debt Representative of the Class A Bonds will have the right to vote and instruct the Issuer Security Trustee, subject to the other provisions of the Intercreditor Arrangements described below (See "*Bondholder Meetings on Intercreditor Matters in a Default Situation*" below). The Issuer and any affiliates will have no right to vote or instruct the Issuer Security Trustee in respect of any Class R Bonds held by them.

Accordingly, prior to a Default Situation, the Class B Bonds and Class R Bonds will not be entitled to be represented in the Issuer Instructing Group; however, the Issuer and Holdings have each covenanted to use their reasonable endeavours to ensure that at all times there is a Qualifying Debt Representative at the Issuer level who is a Financial Guarantor, in order to ensure there is an Issuer Qualifying Debt Representative which is able to provide instructions in a timely manner to the Issuer Security Trustee.

The Intercreditor Arrangements provide that, in approving any disposal of any assets secured by the Guarantor Security, those DCC Secured Creditors making up the Beneficiary Instructing Group or, as the case may be, those Issuer Secured Creditors making up the Issuer Instructing Group, shall be subject to the same duties as would apply in equity to any receiver or mortgagee of those secured assets.

Intercreditor Arrangements at the Issuer Level

The Issuer Security Trustee will be instructed by the Issuer Instructing Group. Prior to a Default Situation, the Issuer Instructing Group will be constituted by the Issuer Qualifying Debt Representatives of the Class A Bonds and any Authorised Loan Facilities (but not the Liquidity Facility Agreements or any Hedging Agreements) provided that the relevant Qualifying Debt Representative (other than the Bond Trustee) has provided an Appropriate Indemnity to the Issuer Security Trustee. After a Default Situation, the Issuer Instructing Group may be constituted, *inter alios,* by the Qualifying Debt Representative of the Class A Bonds, the Class B Bonds and the Class R Bonds. Class C Bonds and Class D Bonds may only be represented by the Bond Trustee in the Issuer Instructing Group where there is no Qualifying Debt Representative in respect of the Class A Bonds, Authorised Loan Facilities, Class B Bonds or Class R Bonds (and, in the case of the Class D Bonds, the Class C Bonds) able to constitute an Issuer Instructing Group.

The Issuer Instructing Group will instruct the Issuer Security Trustee on the basis of one vote for each £1 of their IIG Outstanding Principal Amount at the time the vote is taken. A Financial Guarantor may vote in respect of the IIG Outstanding Principal Amount of the Bonds guaranteed by such Financial Guarantor, provided it is at the relevant time the Issuer Qualifying Debt Representative in respect of such Bonds. See also "*Bondholder Meetings on Intercreditor Matters in a Default Situation*" below.

At the Issuer level, the Issuer Security Trustee will act upon the instructions of the Issuer Qualifying Debt Representative(s) who constitute(s) (either singly or together) more than 50 per cent. of the aggregate IIG Outstanding Principal Amount of the Qualifying Debt. At the DCC level, the Issuer Security Trustee as DCC Qualifying Debt Representative of the Issuer will cast the votes of the Issuer Instructing Group proportionately (see "*Intercreditor Arrangements at the DCC Level*" below).

Intercreditor Arrangements at the DCC Level

The DCC Security Trustee will act as trustee on behalf of the DCC Secured Creditors in connection with the DCC Security and the Guarantor Security. In such capacity, the DCC Security Trustee will agree that it will exercise any right (other than entrenched rights and reserved matters) which it may have in respect of the DCC Transaction Documents only as directed by the Beneficiary Instructing Group.

The definition of Qualified DCC Secured Creditor determines who is able to constitute the Beneficiary Instructing Group. The Issuer Security Trustee will represent the Issuer as part of the Beneficiary Instructing Group and will split its portion of the aggregate BIG Outstanding Principal

Amount of the Qualified DCC Secured Creditors into separate £ for £ amounts (each a "**Proportion**"), and each representing the votes/instructions received by the Issuer Security Trustee from the respective members of the Issuer Instructing Group. The Issuer Security Trustee will not have a vote in respect of any Issuer Secured Creditors who were not holders of Qualifying Debt or otherwise did not vote or instruct the Issuer Security Trustee as part of the Issuer Instructing Group.

It should be noted that, prior to a Default Situation, only the Qualifying Debt Representative of the Class A Bonds and the Authorised Lenders to the Issuer will be capable of constituting a Proportion.

The DCC STID will provide that the DCC Security Trustee will take action only when it has received instructions from a Beneficiary Instructing Group.

Bondholder Meetings on Intercreditor Matters in a Default Situation

In a Default Situation, the Class B Bonds and Class R Bonds will be represented by the Bond Trustee as Qualifying Debt Representative who may convene a meeting of Bondholders (which will be a single meeting of the holders of the Class B Bonds and Class R Bonds) to consider any matter. The Intercreditor Arrangements provide that no such Bondholder meeting will be convened if, within three business days of the Bond Trustee serving notice on the relevant Security Trustee of its intention to convene such a meeting, the relevant Security Trustee confirms that it has already received instructions for or against the relevant matter from more than 50 per cent. of the Intercreditor Parties that could form part of the Issuer Instructing Group or Beneficiary Instructing Group, as the case may be (a "**Confirmation of Instruction**"). If the Bond Trustee receives a Confirmation of Instruction at any time before the day of the relevant Bondholder meeting, it shall notify the Bondholders that the meeting will be cancelled. The Conditions of the Bonds also make provision for Bondholder committees to be constituted (see Chapter 6 under "*Terms and Conditions of the Bonds – Condition 15*").

Emergency Instruction Procedure

During a Default Situation, certain decisions and instructions may be required in a timeframe which does not provide a sufficient period in which to convene Bondholder meetings. To cater for such circumstances, the Intercreditor Arrangements provide for an emergency instruction procedure. The relevant 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 the Qualifying Debt Representatives (the "**EIN Signatories**") representing more than $66^{2}/_{3}$ per cent. of the aggregate BIG Outstanding Principal Amount of the Qualified DCC Secured Creditors, after excluding the proportion in respect of which the Qualifying Debt Representative is a Bond Trustee who is unable to give an instruction (or exercise a vote) on the matter which is the subject of the Emergency Instruction Notice without convening a Bondholder meeting. The Emergency Instruction Notice must specify the emergency action which the relevant Security Trustee is being instructed to take and must certify that, unless such action is taken before the date on which a resolution of Bondholders could first be obtained, the interests of the Qualified DCC Secured Creditors represented by the EIN Signatories will be materially prejudiced.

Entrenched Rights, Reserved Matters and Standstill

The Intercreditor Arrangements are subject to certain entrenched rights and reserved matters. Each DCC Secured Creditor and each Issuer Secured Creditor has certain entrenched rights which cannot be exercised without the consent of the person having such entrenched right (see "*DCC STID – Entrenched Rights*" and "*Issuer STID – Entrenched Rights of Issuer Secured Creditors*" below), and certain reserved matters which such person is free to exercise, notwithstanding the Intercreditor Arrangements.

The Intercreditor Arrangements at the DCC level are modified during a Standstill, in particular in respect of terminating the Standstill Period (see "*DCC STID – Standstill*" below).

Intercreditor Definitions

The following defined terms are used in this document in relation to the Intercreditor Arrangements:

"**Appropriate Indemnity**" means an indemnity in form and substance satisfactory to the relevant Security Trustee.

"**Beneficiary Instructing Group**" will be defined in the DCC STID to mean (except with respect to the termination of any Standstill) Qualified DCC Secured Creditor(s) (as defined below) to whom are owed more than 50 per cent. of the aggregate BIG Outstanding Principal Amount of the Qualified DCC Secured Liabilities (as defined in the DCC STID) at the relevant time.

"**BIG Outstanding Principal Amount**" means on any date in relation to:

(i) the Issuer, the IIG Outstanding Principal Amount voted by the Issuer Security Trustee proportionately (as referred to in paragraph (ii) of the definition of Qualified DCC Secured Creditor);

(ii) any Authorised Loan Facilities provided to DCC, the equivalent amount in the Base Currency of the outstanding principal amount of any drawn amounts;

(iii) each DCC Finance Lease, the highest termination value which may fall due during the annual period encompassing such date and falling between two annual rental payment dates under the relevant Finance Lease (the "**Annual Period**"), calculated upon the assumptions and the cashflow report provided by the relevant DCC Finance Lessor on the first day of each such Annual Period;

(iv) each DCC Hedge Document (as defined in the DCC STID), the amount (if any) that would be payable to the relevant DCC Hedging Counterparty on such date (as defined below) if an Early Termination Date were designated in respect of the transaction or transactions arising thereunder pursuant to Section 6(e) of the ISDA Master Agreement governing such transaction or transactions;

(v) the CfD, the amount (if any) that would be payable to the CfD Counterparty on such date if an Early Termination Date were designated in respect of the transaction under the CfD pursuant to Section 6(e) of the ISDA Master Agreement governing such transaction; and

(vi) any other permitted debt, the equivalent amount in the Base Currency of the outstanding principal amount of such debt in accordance with the relevant underlying documentation.

"**DCC Qualifying Debt Representative**" in respect of the Beneficiary Instructing Group means in relation to:

(i) any Intercompany Loan Agreement, the Issuer Security Trustee;

(ii) any DCC Finance Lease, the relevant DCC Finance Lessor;

(iii) any Authorised Loan Facility provided to DCC, the facility agent acting on the instructions of an instructing group of lenders or, where there is no facility agent, the Authorised Lender under such Authorised Loan Facility;

(iv) any DCC Hedge Document, the relevant DCC Hedging Counterparty;

(v) the CfD, the CfD Counterparty; and

(vi) any other form of permitted debt, the relevant representative appointed under the terms of the relevant underlying documentation.

"**Default Situation**" means any period during which there subsists:

(i) a Standstill;

(ii) an Issuer Event of Default; or

(iii) a DCC Event of Default.

"**FG Event of Default**" means in relation to the Financial Guarantor of the first Series of Class A Bonds:

(i) any Insured Amount which is Due for Payment (each as defined in the relevant Bond Policy (see Chapter 7 under "*MBIA Bond Policy*") is unpaid by reason of non-payment and is not paid by such Financial Guarantor on the date stipulated in the relevant Bond Policy;

(ii) 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;

(iii) such Financial Guarantor:

(a) presents any petition, commences any case or takes any proceedings for the winding-up or the appointment of an administrator or receiver (including an 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;

(b) makes or enters into any general assignment, composition, arrangement (including a voluntary arrangement under Part 1 of the UK Insolvency Act 1986) or equivalent legislation or compromise with or for the benefit of any of its creditors;

(c) has a final and non-appealable order for relief entered against it under any Bankruptcy Law; or

(d) has a final and non-appealable order, judgement 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 possession by a Custodian of such Financial Guarantor,

and shall mean in relation to any further Financial Guarantor such events as described in the relevant Bond Policy or Bond Policies of such Financial Guarantor as defined more particularly in the applicable Pricing Supplement.

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, liquidation, conservation, fraudulent conveyance or similar law, statute or regulation of the French Republic or any other applicable jurisdiction for the relief of debtors.

"**IIG Outstanding Principal Amount**" means on any date in relation to:

(i) the Class A Bonds, Class B Bonds, Class R Bonds, Class C Bonds and Class D Bonds, the equivalent amount in the Base Currency of the aggregate Principal Amount Outstanding (as defined in the Conditions) of the relevant Class or Classes of the outstanding Bonds (including any premium or indexation);

(ii) Authorised Loan Facilities provided to the Issuer, the equivalent amount in the Base Currency of the outstanding principal amount of any drawn amounts; and

(iii) any other permitted debt, the equivalent amount in the Base Currency of the outstanding principal amount of such debt in accordance with the relevant underlying debt documentation.

"**Issuer Instructing Group**" means (except with respect of the termination of any Standstill) the Issuer Qualifying Debt Representatives in respect of Qualifying Debt who, prior to a Default Situation, have provided an Appropriate Indemnity (other than the Bond Trustee) to the Issuer Security Trustee and to whom are owed more than 50 per cent. of the aggregate IIG Outstanding Principal Amount of the Qualifying Debt;

"**Issuer Qualifying Debt Representative**" means in relation to:

(i) the Class A Bonds, until the full and complete payment by the Issuer of all sums due under the Class A Bonds, the relevant Financial Guarantor unless and until:

(a) such time as the Issuer Security Trustee has received notice from the Bond Trustee or the Financial Guarantor that a FG Event of Default has occurred and is continuing (and has not otherwise been waived or cured to the satisfaction of the Bond Trustee); or

(b) notwithstanding the absence of any FG Event of Default, no amounts could become payable by the Issuer to the Financial Guarantor under the Issuer Transaction Documents,

in which case the Qualifying Debt Representative for the Class A Bonds shall be the Bond Trustee on behalf of the Class A Bondholders;

(ii) the Class B Bonds, the Class R Bonds, the Class C Bonds and the Class D Bonds, the Bond Trustee on behalf of the holders thereof (excluding, in the case of the Class R Bonds, the Issuer or any affiliate thereof); and

(iii) any Authorised Loan Facility provided to the Issuer, the facility agent acting on the instructions of an instructing group of lenders in accordance with the terms of such Authorised Loan Facility or, where there is no facility agent, the Authorised Lender under such Authorised Loan Facility.

"**Qualified DCC Secured Creditor**" means:

(i) each Authorised Lender and each DCC Finance Lessor which, prior to a Default Situation, provides an Appropriate Indemnity to the DCC Security Trustee; and

(ii) the Issuer, on whose behalf the Issuer Security Trustee shall vote (provided that, prior to a Default Situation it provides an Appropriate Indemnity in respect of the proportionate votes received by it from the Issuer Instructing Group). In this respect, the Issuer Security Trustee will split its portion of the aggregate BIG Outstanding Principal Amount of the Qualified DCC Secured Creditors into Proportions (as set out above); or

(iii) if none of the above, then the DCC Qualifying Debt Representative (provided, prior to a Default Situation, it provides an Appropriate Indemnity) of the DCC Secured Creditor (or DCC Secured Creditors if more than one such *pari passu* ranking DCC Secured Creditor) who at such time has/have the highest ranking in respect of its/their outstanding principal amount in the applicable DCC Post-Enforcement Payments Priorities.

"**Qualifying Debt**" means the outstanding principal amount of:

(i) the Class A Bonds provided that the Issuer Qualifying Debt Representative is the relevant Financial Guarantor; and

(ii) debt financing provided to the Issuer pursuant to Authorised Loan Facilities (which for the avoidance of doubt will not include any Liquidity Facility Agreements or any Hedging Agreements); and

(iii) where there is either no Qualifying Debt as referred to in (i) and (ii) above or there is a Default Situation or the relevant Financial Guarantor is not the Issuer Qualifying Debt Representative in relation to any Class A Bonds the outstanding Class A Bonds (unless included in (i) above), Class B Bonds and Class R Bonds together (as provided in the Conditions of the Bonds and subject to the provisions of the Issuer STID); or

(iv) where there is no Qualifying Debt as referred to in (i), (ii) or (iii) above, the outstanding Class C Bonds; or

(v) where there is no Qualifying Debt as referred to in (i), (ii), (iii) or (iv) above, the outstanding Class D Bonds; or

(vi) where there is no Qualifying Debt as referred to in (i), (ii), (iii), (iv) or (v) above, any remaining secured liabilities of the Issuer.

"**Qualifying Debt Representative**" means an Issuer Qualifying Debt Representaive and/or a DCC Qualifying Debt Representative, as the case may be.

SUMMARY OF FINANCE DOCUMENTS

Intercompany Loan Agreements

Introduction

The Issuer will on-lend an amount equal to the sterling equivalent of the gross proceeds of issue of each Sub-Class of Bonds of each Series (or, in the case of Class R Bonds, the proceeds of sale of such Sub-Class) to DCC under the terms of an intercompany loan agreement referable to that Series (each such agreement an ''**Intercompany Loan Agreement**''). Such proceeds of each Sub-Class of Bonds of each Series and each drawing under each Authorised Loan Facility available to the Issuer or, in certain circumstances, Liquidity Facility will be used to fund a separate corresponding advance under the corresponding Intercompany Loan Agreement. All advances to be made by the Issuer under each Intercompany Loan Agreement will be in sterling and at rates of interest set out in the relevant Pricing Supplement or, if hedged in accordance with the hedging policy (see ''*Hedging Agreements*'' below) at the hedged rate plus, in each case, a margin.

The Initial Intercompany Loan Agreement

The Intercompany Loan Agreement in respect of the first Series of Bonds will be made between the Issuer, DCC and the Issuer Security Trustee on or before the Initial Issue Date (the ''**Initial Intercompany Loan Agreement**''). Under the terms of the Initial Intercompany Loan Agreement, the Issuer will agree to make available to DCC on the Initial Issue Date:

1. a facility in the aggregate amount of £1,910,000,000 (the ''**Initial Term Facility**'') in eleven tranches, each tranche corresponding to a Sub-Class of the Bonds (''**Tranche A1**'' (in an aggregate principal amount of £350,000,000), ''**Tranche A2**'' (in an aggregate principal amount of £100,000,000), ''**Tranche A3**'' (in an aggregate principal amount of £200,000,000), ''**Tranche A4**'' (in an aggregate principal amount of £265,000,000), ''**Tranche A5**'' (in an aggregate principal amount of £85,000,000), ''**Tranche B1**'' (in an aggregate principal amount of £325,000,000), ''**Tranche B2**'' (in an aggregate principal amount of £100,000,000), ''**Tranche B3**'' (in an aggregate principal amount of £100,000,000), ''**Tranche B4**'' (in an aggregate principal amount of £35,000,000), ''**Tranche C1**'' (in an aggregate principal amount of £125,000,000), ''**Tranche C2**'' (in an aggregate principal amount of £125,000,000) and ''**Tranche D**'' (in an aggregate principal amount of £100,000,000), respectively, and each advance under Tranche A1, Tranche A2, Tranche A3, Tranche A4, Tranche A5, Tranche B1, Tranche B2, Tranche B3, Tranche C1, Tranche C2, Tranche D or any further term advance under any subsequent Intercompany Loan Agreement, is referred to in this Information Memorandum as a ''**Term Advance**''); and
2. a revolving credit facility in an aggregate amount of £370,000,000 divided into:
   - a Tranche R1 facility (''**Tranche R1**'');
   - a Tranche R2 facility (''**Tranche R2**'' and, together with Tranche R1, the ''**R Tranches**''); and
   - a Tranche L facility (''**Tranche L**'' and, together with the R Tranches, the ''**Revolving Tranches**''),

   and each advance under Tranche R1 an ''**R1 Advance**'', each advance under Tranche R2 an ''**R2 Advance''** (and together with each R1 Advance, an ''**R Advance**''), each advance under Tranche L an ''**L Advance**'' and each R Advance and L Advance a ''**Revolving Advance**''.

Further Intercompany Loan Agreements

The Issuer, DCC and the Issuer Security Trustee will enter into a further Intercompany Loan Agreement in respect of each further Series of Bonds and each Authorised Loan Facility available to the Issuer or Liquidity Facility on or before the relevant Issue Date (in respect of such further Series of Bonds) or initial drawdown date (in respect of such Authorised Loan Facility or Liquidity Facility). The terms of each further Intercompany Loan Agreement will be substantially similar to those of the Initial Intercompany Loan Agreement and as described further below.

Initial Term Facility

The proceeds of each Term Advance under the Initial Term Facility (together, the ''**Initial Term Advances**'') will comprise an amount equal to the sterling equivalent of the gross proceeds of the issue of Bonds (other than the Class R Bonds) on the Initial Issue Date after having exchanged the proceeds

of any Sub-Class of Bonds denominated in a currency other than sterling into sterling pursuant to the initial currency exchange under the Currency Hedging Agreements with the Initial Hedge Counterparties in respect of such Sub-Class. The Initial Term Advances will be used by DCC for its general corporate purposes, including to pre-fund reserves in the Debt Service Payment Account and the Reserves Account, to repay all outstanding amounts under the Bridge Facility and to make a loan of up to £459,000,000 to Holdings, which in turn will apply such proceeds in paying to HUH and HSU the consideration due in respect of the purchase of all the ordinary and preference shares of DCC, respectively, from HUH and HSU (see Chapter 10 under "*Holdings/DCC Loan Agreement*"). The repayments due in respect of each Term Advance under the Initial Intercompany Loan Agreement will be set out in the applicable Pricing Supplement.

R Advances under the Initial Intercompany Loan Agreement

The Initial Intercompany Loan Agreement will provide that the Issuer shall, subject to satisfaction of certain conditions, make R Advances to DCC in an aggregate principal amount equal and corresponding to, as the case may be, the Class R Bonds resold by the Issuer at any time or the relevant borrowings by the Issuer under the Initial Authorised Loan Facility available to the Issuer (up to and including, in the case of the Class R Bonds, 31 March 2006 and, in the case of the Initial Authorised Loan Facility, the day before the fifth anniversary of the Initial Issue Date).

Each R1 Advance will be used by DCC to fund working capital and will be credited to DCC's Payments Account (as defined below). Each R2 Advance will be used by DCC to meet its capital expenditure enhancement requirements and will be paid into DCC's Reserves Account and credited to the Capex Reserve Ledger (each as defined below).

The R Tranches will (unless there has been an acceleration of any DCC Secured Liabilities under the DCC STID) be fully revolving and each R Advance, together with accrued interest on that R Advance, will be repayable in full on each DCC Payment Date, up to and including 31 March 2006 or the day before the fifth anniversary of the Initial Issue Date, as the case may be. The proceeds of each repayment of an R Advance thereof will be applied by the Issuer to repurchase (but not cancel) some or all of the Class R Bonds or repay corresponding borrowings by the Issuer under the relevant Authorised Loan Facility, as the case may be, together with accrued interest to the date of repayment.

On 31 March 2006 or the day before the fifth anniversary of the Initial Issue Date, as the case may be, any undrawn commitment under the R Tranches will be cancelled. The R Advances then outstanding shall, to the extent not repaid on such DCC Payment Date (and DCC shall be under a best endeavours obligation to procure that the R Advances are repaid in full on such DCC Payment Date), cease to revolve and shall convert to term advances in respect of which DCC has agreed to use its best endeavours to repay in full as soon as reasonably practicable after such DCC Payment Date. All R Advances must be repaid no later than March 2035.

L Advances under the Initial Intercompany Loan Agreement

The Initial Intercompany Loan Agreement will provide that the Issuer shall (unless there has been an acceleration of any DCC Secured Liabilities under the DCC STID) make L Advances to DCC in an aggregate amount not exceeding the amount available to the Issuer from time to time under the Liquidity Facility with the Initial Liquidity Facility Provider(s). Each L Advance will be used by DCC to meet shortfalls in (a) scheduled payments of interest due in respect of its Authorised Loan Facility and any outstanding Term Advances (other than under Tranche D) and R Advances under the Initial Intercompany Loan Agreement (except that the amount available to meet interest shortfalls in respect of outstanding advances under Tranche C shall be subject to certain limits) and (b) the notional interest element of any scheduled lease payments under the Finance Leases.

The L Advances will be revolving credit advances repayable on each DCC Payment Date under the Initial Intercompany Loan Agreement in accordance with the DCC Standstill Priority (as defined below).

Repayment of Revolving Advances Generally

The Initial Intercompany Loan Agreement will permit DCC and the Issuer to net (prior to the occurrence of an acceleration under the DCC STID) amounts respectively owed to each other under the Initial Intercompany Loan Agreement on any DCC Payment Date (whether by way of repayment of a Revolving Advance or the making of a further Revolving Advance) such that only the net amount remaining after such netting shall fall to be paid. No Revolving Advance may be re-borrowed after the occurrence of an Issuer Event of Default which is continuing under the Bonds or the occurrence of an

event of default which is continuing under any Authorised Loan Facility available to the Issuer or (in the case of any R Advance) after 31 March 2006 or the day before the fifth anniversary of the Initial Issue Date, as the case may be.

"**DCC Payment Date**" means each scheduled date for payment of principal, interest, rental or other amounts under any of the Intercompany Loan Agreements, DCC's Authorised Loan Facilities or the DCC Finance Leases.

Interest and Principal

The Initial Intercompany Loan Agreement will contain provisions for determining the amount of interest payable on each DCC Payment Date in respect of each Term Advance and Revolving Advance (until any such Term Advance and/or Revolving Advance is repaid) (each a "**Scheduled Interest Amount**" and, in aggregate, the "**Scheduled Interest Payment**") and the amount of principal payable on each such date in respect of the relevant Term Advance and/or Revolving Advance (after netting, prior to an acceleration under the DCC STID, in the case of the relevant Revolving Advance, the principal amount of any Revolving Advance to be reborrowed by DCC on such DCC Payment Date) (each a "**Scheduled Principal Amount**" and, in aggregate, the "**Scheduled Principal Payment**"). The basis for accrual of interest for each Term Advance and each Revolving Advance will be set out in the applicable Pricing Supplement.

The Scheduled Interest Payment payable on a particular DCC Payment Date and the Scheduled Principal Payment payable on such date are herein together referred to as the "**Scheduled Payment**". References in this Information Memorandum to a Scheduled Interest Payment, a Scheduled Principal Payment, a Scheduled Interest Amount or a Scheduled Principal Amount includes reference to such amounts as may be re-calculated.

If, on any DCC Payment Date in respect of Tranche CI, Tranche C2 or Tranche D, there are insufficient monies available to DCC to pay the Scheduled Interest Amount in respect of Tranche CI, Tranche C2 or Tranche D, the amount of the insufficiency shall be treated as not having fallen due and will be deferred until the earlier of (i) the next following DCC Payment Date in respect of Tranche CI, Tranche C2 or, as the case may be, Tranche D on which DCC has sufficient funds to pay such deferred amounts (including any interest accrued thereon) and (ii) the DCC Payment Date of the last maturing Term Advance which ranks in priority to Tranche D and, if applicable, Tranche C1, Tranche C2. Interest will accrue on such deferred interest at the rate that would otherwise be payable on Tranche C1, Tranche C2 or, as the case may be, Tranche D.

Fees in respect of Tranche L

Where a Standby Drawing (as defined below) has been made under a Liquidity Facility Agreement, DCC will pay to the Issuer a fee on each Issuer Payment Date in respect of the Standby Drawing in an amount which is equal to the difference between the interest accrued under the relevant Liquidity Facility Agreement on the Standby Drawing and the amount earned by way of investment of the amount representing such Standby Drawing (such amount being referred to as an "**Additional Amount**").

Fees Generally

Under the terms of the Initial Intercompany Loan Agreement, DCC will be required to pay to the Issuer certain facility lending fees in respect of the period to and including the Initial Issue Date, as follows (in no order of priority):

- an amount equal to the upfront fees, costs, charges, liabilities and expenses and any other amounts due and payable by the Issuer to the Bond Trustee pursuant to the Trust Deed and to the Issuer Security Trustee pursuant to the Issuer Deed of Charge and the Issuer STID;
- an amount equal to the upfront fees and expenses of any legal advisers, accountants and auditors appointed by the Issuer, the Issuer Security Trustee or the Bond Trustee which have fallen due and which were incurred under or for the purposes of transactions effected by the Issuer Transaction Documents;
- an amount equal to the upfront premia, fees, costs, charges, liabilities and expenses and any other amounts due and payable to MBIA pursuant to the relevant I&I Agreement (as defined below);

- an amount equal to the upfront fees and expenses of the Co-Arrangers, the Dealers, the Class R Underwriters and financial advisers appointed by the Issuer and the upfront fees and expenses of any legal advisers, accountants or other advisers appointed by any of them;
- an amount equal to the upfront fees, costs and expenses due and payable to the Paying Agents, the Registrar, the Transfer Agents, the Luxembourg Listing Agent, the Agent Bank and any other agents of the Issuer appointed pursuant to the Paying Agency Agreement or otherwise;
- an amount equal to the upfront fees, costs and expenses in respect of the incorporation, organisation and registration of the Issuer in the Cayman Islands and the United Kingdom (other than the first £30,000 which will be payable by the Issuer);
- an amount equal to the upfront fees of the Initial Authorised Lender under the Issuer's Initial Authorised Loan Facility;
- an amount equal to all the upfront fees due and payable to the Initial Liquidity Facility Providers under the terms of the Initial Liquidity Facility Agreement;
- an amount equal to the upfront fees, costs, charges, liabilities and expenses due and payable to the Account Bank pursuant to the Issuer Account Bank Agreement;
- an amount equal to the upfront fees, costs, liabilities, expenses and other amounts incurred or paid or payable by the Issuer in connection with entering into the Hedging Agreements;
- an amount equal to amounts due and payable by the Issuer to Rating Agencies, the Co-Arrangers, the Dealers, the Class R Underwriters or any Authorised Lender (excluding, for these purposes, payment for the benefit of the Bondholders);
- an amount equal to any other amounts due or overdue from the Issuer to third parties (other than government and fiscal authorities) including any which arise directly or indirectly from the funding by the Issuer of the facilities made available under the Initial Intercompany Loan Agreement, other than amounts listed in the above paragraphs; and
- an amount equal to any VAT arising in respect of any of the above amounts listed in the above paragraphs except to the extent such VAT is recoverable by the Issuer or other person on whom the liability to pay such VAT falls.

In respect of the period after the Initial Issue Date, until all obligations of DCC under the Initial Intercompany Loan Agreement have been discharged in full, DCC will be required to pay periodically to the Issuer certain further fees, as follows (in no order of priority):

- an amount equal to the fees, costs, charges, liabilities and expenses and any other amounts due and payable by the Issuer to the Bond Trustee pursuant to the Trust Deed and to the Issuer Security Trustee pursuant to the Issuer Deed of Charge and the Issuer STID from time to time;
- an amount equal to the premia, fees, costs, charges, liabilities and expenses and any other amounts due and payable by the Issuer to MBIA pursuant to the relevant I&I Agreement from time to time;
- an amount equal to the fees and expenses of any legal advisers, accountants and auditors appointed by the Issuer, the Bond Trustee or the Issuer Security Trustee which have fallen due from time to time;
- an amount equal to the fees, costs and expenses due and payable to the Paying Agents, the Registrar, the Transfer Agents, the Luxembourg Listing Agent, the Agent Bank and any other agents of the Issuer appointed pursuant to the Agency Agreement or otherwise from time to time;
- an amount equal to the underwriting fees and expenses of the Dealers and the Class R Underwriters and any legal, accounting and other advisers appointed by them;
- an amount equal to any amounts due and payable by the Issuer to any taxation authority in respect of the Issuer's liability to corporation tax or any other income or similar taxes payable by the Issuer from time to time (insofar as payment cannot be satisfied out of the profits of the Issuer and subject to the terms of the Issuer Deed of Charge and the Issuer STID);

- an amount equal to any fees, costs, expenses or charges imposed or levied on the Issuer by the government of the Cayman Islands and other entities and which are incurred in connection with its registration, maintenance of incorporation and good standing in the Cayman Islands, including the annual fee, registered office provider fee and associated disbursements;
- an amount equal to all amounts of commitment fee and other fees, costs and expenses (other than interest) due or overdue to the Initial Authorised Lender under the Issuer's Initial Authorised Loan Facility and the Initial Liquidity Facility Providers under the terms of the Initial Liquidity Facility Agreement and/or the fees, costs, liabilities and expenses incurred or paid by the Issuer in connection with it entering into any replacement of the Initial Liquidity Facility Agreement;
- an amount equal to the fees, costs, charges, liabilities and expenses due and payable to the Account Bank pursuant to the Issuer Account Bank Agreement from time to time;
- an amount equal to any fees, costs, expenses or other amounts similar to those mentioned above due or overdue to third parties (other than governmental or fiscal authorities) including the Rating Agencies and the amounts paid by the Issuer to the Dealers, the Class R Underwriters and any Authorised Lender (excluding, for these purposes, payment for the benefit of the Bondholders) and which arise directly or indirectly from the funding by the Issuer of the facilities made available under the Intercompany Loan Agreements, other than amounts listed in the above paragraphs;
- an amount equal to any VAT arising in respect of any of the amounts listed in the above paragraphs except to the extent such VAT is recoverable by the Issuer or other person on whom the liability to pay such VAT falls; and
- an amount equal to such amounts as are required by the Issuer to ensure that, having regard to the tax treatment of any of the Issuer's receipts and of any costs and expenses borne by the Issuer, it is able to make full payment of such costs and expenses.

If the Issuer issues further series of Bonds in the future, the fees payable by DCC from time to time may be amended, and the consent of Bondholders thereto will not be sought or obtained.

Indemnity in Favour of Issuer

DCC will also pay, by way of an indemnity, loan or otherwise on each DCC Payment Date, such amounts as are necessary to pay or provide for any liabilities of the Issuer not provided for in the calculation of the Scheduled Payments or otherwise accounted for in the fees referred to above (see "*Fees in respect of Tranche L*" and "*Fees Generally*" above).

Withholding and Deductions – Gross Up

All payments of principal and interest under the Initial Intercompany Loan Agreement will be made free and clear of, and without withholding or deduction for, tax, if any, applicable to such payments in the United Kingdom or any other jurisdiction unless such withholding or deduction is required by law. In that event, DCC will be obliged to pay such additional amounts as will result in the receipt by the Issuer of such amounts as would have been received by it if no such withholding or deduction had been required.

To the extent the Issuer receives a credit or relief from tax as a result of the payment of such additional amounts, the Issuer shall repay such amount to DCC as leaves it in a no better or worse after-tax position than it would have been in had DCC not been required to make such withholding or deduction.

Prepayment

DCC may, subject to the terms of the Common Terms Agreement, prepay any Term Advance, in whole or in part, on any DCC Payment Date in an amount sufficient to enable the Issuer to redeem or prepay (as the case may be) the equivalent amount of Bonds (including any premium payable) and/or any Authorised Loan Facility (including any breakage costs) and the proceeds thereof will be applied by the Issuer in redemption of the whole or part of the equivalent Sub-Class of Bonds in accordance with Condition 8 (see Chapter 6 under "*Terms and Conditions of the Bonds*") and/or prepayment of such Authorised Loan Facility (as applicable). Following any prepayment of a part of any Term Advance or Term Advances or any permanent reduction of a Revolving Advance, DCC shall recalculate the amount of each Scheduled Principal Amount and each Scheduled Interest Amount due

in respect of the relevant Term Advance, Term Advances or Revolving Advance on subsequent DCC Payment Dates as set out above. However, no prepayments of Tranche C1 or Tranche C2 can be made before the next periodic review (and, if that review is appealed, then 1 October 2005) without the prior consent of the DCC Security Trustee (acting on instructions of the Beneficiary Instructing Group).

Conditions Precedent – Term Advances

It will be a condition precedent to the Issuer making the Initial Term Advances available to the Borrower that on the Initial Issue Date the following conditions are satisifed, *inter alia*:

- the Issuer has received the proceeds of the Bonds issued on the Initial Issue Date;
- no Potential Trigger Event or Trigger Event (each as defined below) has occurred which is continuing;
- no potential DCC Event of Default or DCC Event of Default has occurred and is continuing; and
- all the DCC Warranties, Holdings Warranties, HUH Warranties, Glas Securities Warranties and Glas Warranties (each as defined in the Common Terms Agreement and as summarised below) to the extent the same are repeated are true and correct in all material respects.

Similar conditions precedent will apply to any further Term Advances made under any further Intercompany Loan Agreement(s).

Conditions Precedent – Revolving Advances

In addition to the conditions precedent set out above, it will be a condition precedent to the Issuer making any Revolving Advance to DCC under the Initial Intercompany Loan Agreement that each of the Issuer and the Issuer Security Trustee (in the case of the Issuer Security Trustee by means of receipt of a certificate from the Issuer or DCC, as the case may be) is satisfied on the drawdown date for each such Revolving Advance that, *inter alia*:

- in the case of each R Advance, the relevant Class R Bonds have been resold or the relevant drawing under an Authorised Loan Facility has been made and the proceeds received by or on behalf of the Issuer;
- in the case of each L Advance, the relevant Liquidity Facility Agreement has been entered into and the proceeds of a drawing thereunder have been received by or on behalf of the Issuer or released, in the case of a Standby Drawing, from the Initial Liquidity Account; and
- no Issuer Event of Default under the Bonds has occurred and is continuing.

Payments Priorities

The Issuer's right to receive payments under the Initial Intercompany Loan Agreement will be subject to the cash allocation procedures set out in the Common Terms Agreement and, in particular, following the occurrence of a Standstill (as defined below), the DCC Standstill Priority and, following the service of an enforcement notice, the DCC Post-Enforcement Payments Priorities as set out in the DCC STID (see "*Common Terms Agreement*", "*DCC STID*" and "*DCC Cash Management*" below).

Incorporation of Common Terms

Each Intercompany Loan Agreement will be subject to the Common Terms Agreement which will set out, *inter alia*, the representations and warranties, covenants and events of default or termination events which will apply to DCC under, *inter alia,* each Intercompany Loan Agreement and, in the case of HUH (until completion under the Share Purchase Agreement), Holdings and (from completion under the Share Purchase Agreement) Glas and Glas Securities, the representations and warranties, covenants and enforcement events under the DCC Security Documents to which they are a party (see "*Common Terms Agreement*" below).

Common Terms Agreement

Each of the Finance Lessors, the Existing DCC Hedge Counterparty, the Account Bank, the DCC Security Trustee, DCC, the Initial Authorised Lender, the Issuer, Holdings, WPD Finance, HUH (in respect of its rights and obligations until completion under the Share Purchase Agreement), Glas Securities and Glas (in respect of their rights and obligations from completion under the Share Purchase Agreement) will, on or before the Initial Issue Date, enter into a common terms agreement

(the "**Common Terms Agreement**"). The Common Terms Agreement will set out the representations, warranties, covenants (positive, negative and financial) and events of default which will apply to each Intercompany Loan Agreement, each Authorised Loan Facility available to DCC, the Finance Leases and the Gen Re Swap (each as supplemented and amended thereby), the DCC Security Documents (as defined below) and each other agreement between or in respect of DCC and any of the Issuer, the DCC Finance Lessors, the Initial Authorised Lender, the Existing DCC Hedge Counterparty, WPD Finance, the Account Bank, the DCC Security Trustee, the Standstill Cash Manager and any Additional Beneficiary as defined therein (the "**DCC Secured Creditors**"). The Common Terms Agreement will also set out the cash management arrangements to apply to DCC (see "*DCC Cash Management*" below) for so long as there has been no acceleration of liabilities against DCC or for so long as no Standstill Period subsists. Upon the completion of the transfer of shares in Holdings to Glas Securities under the Share Purchase Agreement, Glas Securities and Glas will each assume obligations pursuant to, and HUH will be released from its obligations pursuant to the Common Terms Agreement (and certain other DCC Transaction Documents which incorporate the provisions thereof) without prejudice to the rights of other parties accrued pursuant thereto. It is a requirement of the Common Terms Agreement that certain future providers of Permitted Indebtedness (as defined below) must also accede to the Common Terms Agreement.

A summary of the representations, warranties, covenants and events of default included in the Common Terms Agreement is set out below.

DCC Representations and Warranties

On the Initial Issue Date (subject to agreed exceptions), and (subject to other agreed exceptions) on each subsequent Issue Date and each DCC Payment Date, DCC will make a number of representations and warranties in respect of itself to the DCC Secured Creditors. These representations and warranties of DCC will include (subject, in some cases, to agreed exceptions and qualifications as to materiality and reservations of law) representations and warranties as to:

- its corporate status, power and capacity (a) to enter into and perform its obligations under the DCC Transaction Documents and certain other material contracts and (b) to own its property and assets and to carry on its business;
- its obligations under the DCC Transaction Documents and certain other material contracts being its legal, valid and binding obligations;
- its entry into and performance under the DCC Transaction Documents and certain other material agreements not conflicting with any material agreements to which DCC is a party, its constitutional documents or applicable law;
- the preparation of its financial statements in accordance with applicable accounting standards;
- the validity and admissibility in evidence of the DCC Transaction Documents in any proceedings in England and Wales;
- the claims of the DCC Secured Creditors under the DCC Transaction Documents ranking at least equally with the claims of unsecured creditors of DCC;
- DCC not being in breach of, *inter alia*, the Licence or certain contracts to which it is party;
- DCC's compliance with all applicable laws (including environmental law);
- there being no encumbrances or indebtedness except as permitted under the DCC Transaction Documents;
- no potential DCC Event of Default, DCC Event of Default, Potential Trigger Event or Trigger Event having occurred which is continuing;
- the obtaining by DCC of all relevant consents and approvals;
- DCC's ownership of the assets over which security interests under the DCC Security Documents have been created;
- the maintenance of insurances;
- DCC not being aware of any default by other parties to the DCC Transaction Documents and to certain material contracts of their obligations thereunder;

- the accuracy of certain written information provided by DCC and the accuracy of this Information Memorandum;
- there being no insolvency event in relation to DCC (including special administration); and
- the sole ownership of DCC by Holdings.

"**DCC Security Documents**" means the DCC STID, the DCC Deed of Charge, the Holdings Deed of Charge, (from completion of the Share Purchase Agreement) the Glas Securities Deed of Charge and the Glas Deed of Charge and (until completion under the Share Purchase Agreement) the HUH Deed of Charge and any other document agreed by DCC and the DCC Security Trustee to be a DCC Security Document.

"**DCC Transaction Documents**" includes the Common Terms Agreement, the DCC Security Documents, the Intercompany Loan Agreements, DCC's Authorised Loan Facilities, the DCC Finance Leases and related agreements (including the Supply Agreements, as defined below and the Existing DCC Hedging Agreement), the DCC Hedge Documents, the CfD, the Holdings/DCC Loan Agreement, the DCC Account Bank Agreement and related bank mandates in respect of the DCC Accounts, the facility letter in respect of the Overdraft Facility (as defined below) and any relevant documents entered into by DCC with any Additional Beneficiaries.

"**Material Entity Event**" means certain defaults under certain material contracts in respect of a counterparty to such contracts including non-payment, misrepresentation, breach of obligation, insolvency events, failure to comply with final judgement, illegality and non-compliance where, in each case, such default would be reasonably likely to have a Material Adverse Effect (as defined below).

Guarantor Representations and Warranties

Each of HUH, Holdings, Glas Securities and Glas (as applicable) will also give representations and warranties in favour of the DCC Secured Creditors on each Issue Date and on each DCC Payment Date (in the case of HUH, only until completion of the Share Purchase Agreement). The representations and warranties to be given by each of them will include (subject, in some cases, to agreed exceptions and, in relation to HUH only, qualifications as to materiality) representations and warranties as to:

- its corporate status, power and capacity (a) to enter into and perform its obligations under the DCC Transaction Documents and (b) to own its property and assets and to carry on its business;
- its obligations under the DCC Transaction Documents being its legal, valid and binding obligations;
- its entry into and performance of its obligations under the DCC Transactions Documents not conflicting with any material agreements to which it is a party, its constitutional documents or applicable law;
- no proceedings having been commenced or threatened;
- the validity and admissibility in evidence of the DCC Transaction Documents to which it is a party in any proceedings in England and Wales;
- the claims of the DCC Secured Creditors' under the Guarantor Security to which it is a party ranking at least equally with the claims of its unsecured creditors;
- its compliance with all applicable laws;
- (except in the case of HUH) there being no encumbrances or indebtedness except as permitted under the DCC Transaction Documents;
- so far as it is aware, no potential DCC Event of Default, DCC Event of Default, Potential Trigger Event or Trigger Event having occurred which is continuing;
- the obtaining by it of all relevant consents and approvals;
- its ownership of the assets over which security interests under the Guarantor Security to which it is a party have been created; and
- there being no insolvency event in relation to it.

DCC Covenants – positive

Subject to agreed exceptions and materiality qualifications, DCC will give certain covenants in favour of the DCC Secured Creditors, including customary covenants relating to maintenance of legal validity and legal status, maintenance of its insurances, compliance with environmental laws and maintenance of any necessary environmental permits, compliance with DCC's obligations with respect to cash management, notification of potential DCC Events of Default and DCC Events of Default, ranking of claims, compliance with consents and approvals necessary for the conduct of its business (including the leasing of the Equipment (as defined below)), notification of material litigation, timely payment of outgoings and taxes, the preparation of accounts and adequacy of systems, further assurance, perfection and protection of security interests under the DCC Security Documents. In addition, DCC will undertake, *inter alia*, to:

- notify the DCC Security Trustee, the Issuer Security Trustee, the other DCC Secured Creditors and the Issuer Secured Creditors other than the Bond Trustee in writing of the occurrence of:

  - any Potential Trigger Event, Trigger Event, potential DCC Event of Default or DCC Event of Default; and

  - any event which would reasonably be expected to give rise to a material claim; or

  - any other event which has a Material Adverse Effect,

  in each case as soon as reasonably practicable upon becoming aware of such event;

  ''**Material Adverse Effect**'' means a material adverse effect (taking into account the timing and availability of any rights and remedies under the WIA or the Licence) on (a) the business, operations, property or financial condition of DCC; or (b) the ability of DCC to perform its obligations under the DCC Transaction Documents, certain material contracts or the Licence; or (c) the validity or enforceability of the DCC Transaction Documents, certain material contracts, or the rights or remedies of the DCC Secured Creditors or DCC thereunder; or (d) the ability of DCC to carry on the business of a water and sewerage undertaker.

- deliver to the DCC Secured Creditors promptly after any reasonable request therefor made by the Issuer Security Trustee, a certificate signed on its behalf by an authorised signatory of DCC (a) confirming that no Potential Trigger Event, Trigger Event, potential DCC Event of Default or DCC Event of Default has occurred since the date of the last such certificate setting out details of any such event which has occurred (other than those previously notified) and of which it is aware having made all reasonable enquiries, and of any action taken or proposed to be taken to remedy such event, and (b) dealing with such other matters in relation to which the Issuer Security Trustee may reasonably require to be satisfied or to receive information for the purposes of the Common Terms Agreement;

- provide the Investor Reports and other information as set out in Chapter 1 under ''*Investor Information*'';

- provide the Director General of Water Services (the ''**DGWS**'') with all information required by him in accordance with the Licence on a timely basis;

- use all reasonable endeavours to procure that the DCC Security Trustee is joined in the consultation process with the DGWS if DCC becomes subject to any transfer scheme (as defined in the WIA);

- not make any Restricted Payments (as defined below) and only to the extent of the balance in the Customer Payments Account unless:

  - no drawings are outstanding under Tranche R1, the Overdraft Facility or any other Authorised Loan Facility provided directly to DCC by any Authorised Lender to the extent that such drawings relate to working capital requirements;

  - the balance on the Debt Service Payment Account on the required date is not less than the required debt service payment account balance for the time being;

  - the backward looking and forward looking ICR is greater than or equal to 2.0:1 after taking into account the effect of the proposed Restricted Payment;

- the RAR is less than or equal to 0.90:1 after deducting the proposed Restricted Payment from available cash;
- no Standstill is continuing; and
- no Potential DCC Event of Default, DCC Event of Default, Potential Trigger Event or Trigger Event is subsisting.

"**Restricted Payment**" means (i) any dividend or distribution by DCC (other than (a) immediately following completion of the Share Purchase Agreement provided that no Trigger Event or DCC Event of Default has occurred and is continuing (b) required by Holdings because the consideration payable by it to HUH for the shares in DCC is greater than £459 million or required by Glas Securities to pay any consideration greater than £1 under the Share Purchase Agreement and (c) any dividends paid to Holdings which are effectively set off under the Holdings/DCC Loan Agreement so that on a net basis no payment of cash is made by DCC to Holdings) (ii) the payment of any rebate to any customer of DCC made by or on behalf of DCC and (iii) any revenue of DCC voluntarily foregone by it as a result of setting charges below those allowed under its price cap as determined from time to time.

- ensure that it has adequate financial and management resources to enable it to discharge its core obligations under the Licence and under the DCC Transaction Documents and, in respect of performance obligations which are passed down to certain material Contractors, it has retained sufficient control to discharge its obligations under the Licence and the DCC Transaction Documents;
- enter into and comply with hedging arrangements in accordance with the agreed hedging policy;
- ensure that the nature of its business is limited to performing the functions of a water and sewerage undertaker as defined in the WIA (the "**Permitted Business**");
- operate, maintain and conduct its business in accordance with, *inter alia*, the Licence, the WIA and its constitutional documents;
- procure that any future outsourcing contracts comply with public procurement rules and that they shall comply with the Outsourcing Policy;

  "**Outsourcing Policy**" means the schedule of provisions and procedures to be applied by DCC in the course of procuring and entering into any further outsourcing agreements, to be reviewed and amended from time to time in accordance with DCC's Procurement Plan (as defined below) and good industry practice.

- maintain a majority of non-executive directors (not being employees of any member of the Financing Group or, after completion under the Share Purchase Agreement, the Glas Group) on its board of directors;
- use its reasonable endeavours (to the extent it is within its control to do so) to maintain the shadow credit rating of the Class A Bonds and the credit rating of the Class B Bonds and Class R Bonds at investment grade or better with any two of the Rating Agencies; and
- in the event that any of the Local Authority Loans becomes, pursuant to its terms, capable of being declared due and payable prior to its scheduled payment date, DCC shall, within the agreed time period or, if earlier, by no later than the day on which such Local Authority Loan is declared to be due and payable, repay such Local Authority Loan in full.

"**Local Authority Loans**" means the local authority loans referred to in "*Additional Resources Available*" below.

In respect of each of the above covenants requiring any action or discretion on the part of the DCC Security Trustee, the DCC Security Trustee will only act under instructions of the Beneficiary Instructing Group in accordance with the DCC STID.

DCC Covenants – negative

Subject to agreed exceptions and materiality qualifications, DCC will undertake, among other things, not to:

- change its tax residence from the United Kingdom or (unless otherwise permitted under the DCC Transaction Documents) surrender any tax losses or allowances on other than arm's length terms;
- permit or agree to any suspension or abandonment of all or a material part of its business except in accordance with the provisions of the WIA;
- create or permit to subsist any encumbrance over all or any of its present or future revenue, leased Equipment or assets other than a Permitted Encumbrance. "**Permitted Encumbrances**" will include: (a) specified existing encumbrances; (b) certain encumbrances over after-acquired assets which are discharged within the agreed time or in respect of which the holder becomes a party to the DCC STID; (c) encumbrances under finance leases and similar agreements where the counterparty becomes a party to the DCC STID; (d) certain encumbrances arising in favour of the Account Bank; and (e) any other encumbrances (not within the specified categories of Permitted Encumbrances) provided that the aggregate principal amount secured by such encumbrances does not exceed £10,000,000 (indexed) and provided further that, in the case of any encumbrance under (a), (b), (c), (d) or (e) above, such encumbrance does not contravene the WIA, the Licence or any requirements thereof;
- make any loans, grant any credit or other financial accommodation or give any guarantee to or for the benefit of any person or otherwise voluntarily assume any liability in respect of any obligation of any other person (except under the DCC/Holdings Loan Agreement and certain other agreed exceptions) other than Permitted Indebtedness (as defined below) provided that no DCC Event of Default or Potential DCC Event of Default is subsisting at the time such Permitted Indebtedness is proposed to be made or would result from such indebtedness;
- incur, create or permit to subsist or have outstanding any indebtedness for borrowed money other than Permitted Indebtedness. "**Permitted Indebtedness**" will include indebtedness for borrowed money incurred (a) which ranks *pari passu* with Advances made under an Intercompany Loan Agreement from the proceeds of issue of Class A, Class B, Class R or Class C Bonds, if the financial ratio tests in respect of the raising of new debt described in "*DCC Covenants – Financial*" below would be met after incurring such indebtedness or, if they would not be met, the additional requirements in respect of the raising of new debt described in "*DCC Covenants – Financial*" would be met and (b) which is subordinated either pursuant to the Issuer STID (or the DCC STID in relation to any indebtedness under the Intercompany Loan Agreements) such that it ranks subordinate to any Class C Bonds or, as the case may be, any advance made under an Intercompany Loan Agreement from the proceeds of issue of Class C Bonds;

  "**DCC Finance Leases**" means the Finance Leases and, provided that the incurrence of further indebtedness under any further finance lease would not result in any breach of the financial ratios described in "*Financial Covenants*" below, any further finance lease provided the aggregate notional principal amount outstanding of the Finance Leases and all such further finance leases does not exceed £360,000,000;
- make any disposal of the whole or any part of its revenues or its assets, leased Equipment or its business or undertaking other than Permitted Disposals. "**Permitted Disposals**" will include certain disposals (a) on arm's length terms of assets in the ordinary course of trade or in connection with arm's length transactions entered into for *bona fide* commercial purposes for the benefit of the Permitted Business, (b) of obsolete or surplus assets, (c) of protected land made in accordance with the Licence, (d) of leased Equipment pursuant to a DCC Finance Lease, (e) pursuant to the Asset Sale Agreement referred to in Chapter 10 under "*Asset Sale Agreement*" (f) provided that the consideration received by DCC in respect of the relevant disposal when aggregated with all other disposals by it made in the immediately preceding twelve month period does not exceed 2.5 per cent. of RAV (as defined below) for the time being and (g) that are Restricted Payments which are permitted to be made;

- merge or consolidate with any other person or participate in any other type of corporate reconstruction without the prior written consent of the DCC Security Trustee (acting on the instructions of the Beneficiary Instructing Group) and, other than Permitted Acquisitions, acquire any shares, assets, leased Equipment or form or enter into any partnership, consortium, joint venture or other like arrangement. "**Permitted Acquisitions**" will include acquisitions of assets made (a) in the ordinary course of trade or in connection with arm's length transactions entered into for *bona fide* commercial purposes in furtherance of DCC's statutory obligations, (b) in accordance with the agreed capital expenditure plan and (c) to replace surplus or obsolete assets;

- to the extent its agreement is required for the same, agree any variation to the Licence which would reasonably be expected to have a Material Adverse Effect;

- unless permitted under the DCC STID and the Common Terms Agreement pay, prepay or repay or defease, exchange or purchase any amount under any loan or other indebtedness subordinated to its obligations under the DCC Transaction Documents or redeem or repurchase any of its share capital;

- enter into any treasury transaction which is not a Permitted Treasury Transaction. A "**Permitted Treasury Transaction**" will include (a) a transaction entered into accordance with the agreed hedging policy, (b) the Gen Re Swap and (c) certain foreign exchange transactions entered into in the ordinary course of business;

- dispose of assets on a sale and leaseback basis or any of its receivables on recourse terms or in relation to a securitisation (except for factoring and the discounting of bills and notes in the ordinary course of its business) unless the resulting indebtedness is Permitted Indebtedness and provided that, in any such case, the consideration in respect of such sales, leases, transfers or disposals is received in cash payable in full at the time and does not exceed the agreed threshold in aggregate at any time; or

- have greater than 20 per cent. of its aggregate nominal outstanding external indebtedness for borrowed money fall due for scheduled final repayment within any 24 month period.

Other covenants (subject to agreed exceptions and materiality qualifications) given by DCC will include covenants relating to the operation and abandonment of its business, not to create or acquire subsidiaries, not to enter into any arrangement or contract with any of its affiliates or any entity otherwise than on arms' length terms, not to amend its constitutional documents, certain material contracts, or the Licence, and not to compromise or settle any material claim without prior notification to the DCC Security Trustee, the other DCC Secured Creditors and the Issuer Secured Creditors.

DCC will periodically certify to the DCC Secured Creditors and indirectly to the Issuer Secured Creditors whether it is in compliance with its obligations under the DCC Transaction Documents (and whether a DCC Event of Default or potential DCC Event of Default has occurred). The DCC Security Trustee and the Issuer Security Trustee shall not be responsible for monitoring such compliance by DCC except, in the case of the Issuer Security Trustee (in its role as Qualifying Debt Representative), by means of receipt from DCC of such certificates of compliance pursuant to the provisions of any Intercompany Loan Agreement and shall be entitled to assume until receipt of express notice to the contrary that no such breach, DCC Event of Default or potential DCC Event of Default has occurred.

In particular, where a DCC Event of Default, covenant, representation or warranty refers to Material Adverse Effect, material adverse change, materiality or like terminology, the DCC Security Trustee and the Issuer Security Trustee (including in its role as Qualifying Debt Representative) will not determine such matters (or the absence thereof). The Issuer Instructing Group or the Beneficiary Instructing Group (as the case may be) may instruct the Issuer Security Trustee or the DCC Security Trustee (as applicable) whether any such breach by DCC, DCC Event of Default or potential DCC Event of Default has occurred. The Issuer Security Trustee or the DCC Security Trustee shall be bound to act on such instructions in accordance with the Issuer STID or DCC STID (as the case may be). Where the Issuer Instructing Group consists of the Bond Trustee acting on behalf of the relevant Bondholders as referred to in the Issuer STID, the Bond Trustee will not determine Material Adverse Effect, material adverse change, materiality or like terminology, but will instead seek that such determination be made by such relevant Bondholders by means of an Extraordinary Resolution (see Condition 3(h) in Chapter 6 under *"Terms and Conditions of the Bonds"*).

DCC Covenants – Financial

Among the covenants which DCC will make in favour of the DCC Secured Creditors under the Common Terms Agreement, DCC will also undertake to maintain certain financial ratios and take certain actions in the event that such financial ratios fall below specified levels.

The two key financial ratios which DCC will be required to comply with are as follows:

- **Interest Cover Ratio**

  The interest cover ratio (''**ICR**'') will be calculated on a backward-looking basis for the previous financial year and projected on a forward-looking basis for the current financial year and for each future financial year until the next periodic review. DCC will be required to maintain each of these backward-looking and forward-looking ratios at a level of at least 1.6:1. This ratio comprises the amount of Net Cash Flow (as defined below) from operations for a financial year to the amount of Net Debt Service (as defined below) for the relevant financial year.

- **Regulated Asset Ratio**

  The regulated asset ratio (''**RAR**'') will also be calculated on a backward-looking basis as at the previous financial year end and projected on a forward-looking basis for each financial year end date until the next periodic review. Each of these ratios will be subject to a maximum level of 0.95:1 which DCC will covenant to maintain. This ratio represents Total Net Indebtedness (as defined below) of the Glas Group (other than Class D Bonds) as at a date to RAV as at such date.

''**Calculation Date**'' means each 31 March and 30 September in each year starting on 30 September 2001.

''**Net Debt Service**'' means, in relation to a financial year, an amount equal to the aggregate of all interest payable on the Issuer's obligations under and in connection with the Class A Bonds, the Class B Bonds and the Class R Bonds (together ''**Senior Bonds**''), DCC's obligations under and in connection with the DCC Finance Leases and any other senior debt of any member of the Glas Group during such financial year less all indexation on any such liabilities to the extent included in the interest payable on such liabilities during such financial year, all interest receivable by any member of the Glas Group from a third party during such financial year except to the extent included in Net Cash Flow and excluding amortisation of the costs of issue of any Senior Bonds for such financial year.

''**Net Cash Flow**'' means, in respect of a financial year, an amount equal to the actual pre-tax operating profit (after adding back depreciation, any exceptional items, any customer rebates, any infrastructure renewals charge and any impairment of fixed assets written off and deducting any amortisation of fixed asset grants and contributions (as such terms are used in, and each case calculated in accordance with the methodology used in, the most recent financial statements of the Glas Group)) of the Glas Group (on a consolidated basis) for such financial year.

''**RAV**'' means, in relation to a Calculation Date, the regulated asset value for such Calculation Date as last determined by Ofwat (interpolated as necessary) and adjusted as appropriate for out-turn inflation.

''**Total Net Indebtedness**'' means, as at any date, all the Issuer's nominal debt outstanding under and in connection with the Bonds (excluding any Class D Bonds) and any other indebtedness for borrowed money of the Glas Group (on a consolidated basis) including all principal indexation on any such liabilities which are indexed together with any accrued but unpaid interest but after adding back any costs of the issue of or premia associated with the Bonds (excluding any Class D Bonds) (to the extent such costs or premia are not already included in the nominal debt outstanding under and in connection with the Bonds) and less cash (excluding an amount equal to any customer rebate declared by DCC for the following year to the extent that there are funds in the Customer Payment Account to pay such a rebate) and cash investments.

Both the ICR and the RAR relate to the Glas Group on a consolidated basis and will be calculated on a backward-looking basis and projected on a forward-looking basis on each Calculation Date.

If the ICR falls below 1.75:1 or the RAR rises above 0.925:1 then DCC will be required to apply to the DGWS for an interim determination on any available grounds (see Chapter 8 under ''*Interim Determinations of K*'' for further details on interim determinations).

Whenever DCC seeks an interim determination or there is a periodic review, it must apply to the DGWS for a determination which will allow it to maintain a minimum credit rating in the A category for Class B and Class R Bonds and a minimum "shadow" credit rating in the A category for Class A Bonds.

There is flexibility to alter the ratio threshold levels and the minimum and maximum levels specified above for these financial ratios with the agreement of the DCC Security Trustee and additionally provided that two of the Rating Agencies confirm that the alteration will not lead to a downgrade of the rating for any of the Bonds (other than Class D Bonds) below their respective ratings on the date of their original issue.

DCC will not be permitted to raise new debt (other than debt which is subordinate to Class C Bonds) unless it meets certain ratio tests (subject to an exception). To raise new senior debt, the RAR and Senior RAR (as defined below and each calculated on the basis of taking into account such proposed senior debt) must be equal to or less than the levels specified in the tables below for the current and each future financial year until the next periodic review. To raise new debt ranking *pari passu* with Class C Bonds (calculated on the basis of taking into account such proposed debt), the RAR must be equal to or less than the levels specified in the relevant table below for the current and each future financial year until the next periodic review.

Maximum Senior RAR (%) at 31 March

2002	2003	2004	2005	2006	2007	2008	2009	2010	After
78.0	77.5	77.0	76.5	76.0	75.5	75.5	75.0	75.0	75.0

Maximum RAR (%) at 31 March

2002	2003	2004	2005	2006	2007	2008	2009	2010	After
89.0	88.5	88.0	88.0	87.5	87.5	87.0	87.0	86.5	86.0

If these ratio levels would be breached, DCC will only be permitted to raise new debt if:

- two of the Rating Agencies confirm that the raising of the proposed new debt will not result in any Bonds (other than any Class D Bonds) being rated below the rating at the time the Bonds were issued; and
- the consent of the DCC Security Trustee to the raising of the proposed new debt has been obtained.

"**Senior RAR**" means the ratio of Senior Total Net Indebtedness to RAV.

"**Senior Total Net Indebtedness**" means, as at any date, all the Issuer's nominal debt outstanding under and in connection with the Senior Bonds and DCC's nominal debt outstanding under and in connection with the DCC Finance Leases and any other senior debt including all principal indexation on any such liabilities which are indexed together with any accrued but unpaid interest but after adding back any costs of the issue of or premia associated with the Senior Bonds (to the extent such costs or premia are not already included in the nominal debt outstanding under and in connection with the Senior Bonds) and less cash (excluding an amount equal to any customer rebate declared by DCC for the following year to the extent that there are funds in the Customer Payment Account to pay such a rebate) and cash investments.

Guarantor Covenants

Under the Common Terms Agreement, each Guarantor (in the case of HUH until completion under the Share Purchase Agreement and, in the case of Glas and Glas Securities, from completion under the Share Purchase Agreement, and subject, in the case of HUH, to agreed materiality qualifications) will covenant in favour of the DCC Secured Creditors, *inter alia*, to provide the DCC Security Trustee, the other DCC Secured Creditors and the Issuer Secured Creditors with certain financial and other information, to pay all taxes due in a timely manner, to comply with all laws, all DCC Transaction Documents to which it is a party and to notify the DCC Security Trustee of any potential DCC Event of Default or DCC Event of Default under the Common Terms Agreement of which it becomes aware. In addition, each Guarantor (other than HUH) will covenant, *inter alia*, not to carry on any business other than that of a holding company (provided that Holdings shall be permitted to enter into and perform its obligations under the Holdings/DCC Loan Agreement), incur any liabilities, permit any encumbrance to subsist or have any employees or premises (subject to such exceptions as may be required to enable Glas or, as the case may be, Glas Securities to conduct its permitted business) or acquire or establish any further subsidiaries (excluding in the case of Glas any

subsidiaries ("**Relevant Subsidiaries**") as may be required for the sole purpose of (i) acquiring Bonds of any Class issued from time to time by the Issuer after the Initial Issue Date and issuing preference shares to any person and/or subscribing for preference shares issued by another Relevant Subsidiary; and (ii) entering into documentation relating to the same (including put and call options with any holder of any preference shares or any trustee on behalf of such holder)).

Trigger Events

The Common Terms Agreement will also set out certain trigger events (the "**Trigger Events**"), the occurrence of which will enable the DCC Security Trustee, acting on the instructions of a Beneficiary Instructing Group, to require DCC to take certain remedial action. The specific Trigger Events and the consequences which flow from the occurrence of those events (the "**Trigger Event Consequences**", as described more particularly at "*Trigger Event Consequences*" below) are summarised below.

Trigger Events

The occurrence of any of the following events will be a Trigger Event for the purposes of the DCC STID:

1. **ICR and RAR**

   On any Calculation Date:

   (i) the ICR for the previous financial year or for any financial year up to the next periodic review is or is estimated to be less than 2.0:1;

   (ii) the RAR for the previous financial year or for any financial year up to the next periodic review is or is estimated to be more than 0.90:1; or

   (iii) the ICR (adjusted to deduct actual or planned capital maintenance expenditure from the numerator) is less than 1:1.

   See "*DCC Covenants – Financial*" above for further details of the financial ratios referred to above.

2. **Credit Rating Downgrade**

   (i) the shadow credit rating of the Class A Bonds by any two of the Rating Agencies falls to BBB, Baa2 or BBB respectively or below;

   (ii) the credit rating of the Class B Bonds or Class R Bonds by any two of the Rating Agencies falls to BBB, Baa2 or BBB respectively or below; or

   (iii) the credit rating of the Class C Bonds by any two of the Rating Agencies falls below investment grade.

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

3. **Debt Service Payment Account Shortfalls**

   The failure to maintain the required credit balance in the Debt Service Payment Account on the required day.

4. **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 DGWS in the last periodic review in respect of DCC 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 DCC is entitled to make an application for an Interim Determination shall be ignored for the purposes of determining if the 10 per cent. threshold deviation level has been breached.

5. **Capex Reserve Shortfalls**

   As at any Calculation Date, the aggregate of (i) the amount credited to the Reserves Account and (ii) the undrawn commitment under (a) Tranche R2 under the Initial Intercompany Loan Agreement and any replacement or supplemental facility provided for capital expenditure under any further Intercompany Loan Agreement and (b) any Authorised Loan Facility made available to DCC for capital expenditure ((i) and (ii) together, the "**Capex Reserve Facility Amount**") is less than the amount (the "**Net Capex Requirement**") equal to the difference between (x) the forecast

capital expenditure requirement of DCC for the twelve months following such Calculation Date and (y) the amount of operating cashflow forecast as at such Calculation Date to be available to fund such capital expenditure during such twelve month period and the Capex Reserve Facility Amount is less than the Net Capex Requirement on the date which is two months after such Calculation Date.

6. **Drawdown on Liquidity Facility**

The Issuer draws down under any Liquidity Facility (except for the purpose of making a Standby Drawing).

7. **Enforcement Orders**

The making of any Enforcement Order (as defined in the WIA) under Part II, Chapter II of the WIA against DCC which would reasonably be expected to lead to the loss of the Licence or a material fine being levied against DCC.

8. **Circumstances leading to a Special Administration Order**

Any indication arising from notices and/or correspondence issued by, or during correspondence with, Ofwat or any other circumstance of which DCC is aware that would reasonably be expected to lead to an application by the DGWS or the Assembly (as defined below) for a special administration order to be made in respect of DCC.

9. **Termination of Licence**

The giving of a notice to terminate DCC's Licence under the WIA.

10. **Event of Default**

A DCC Event of Default occurs which is continuing.

11. **Material Entity Event**

A Material Entity Event occurs which is continuing.

Trigger Event Consequences

Following the occurrence of a Trigger Event and at any time until such Trigger Event has been waived by the DCC Security Trustee, remedied in accordance with Trigger Event Remedies (as described below) or otherwise remedied to the satisfaction of the DCC Security Trustee, the provisions set out below shall apply:

1. **No Restricted Payments**

DCC shall not make any Restricted Payments and, in respect of customer rebates, if these have not yet been implemented, shall stop their implementation and shall not declare any customer rebates.

2. **Further Information and Remedial Action**

(i) DCC shall provide such information as to the relevant Trigger Event (including its causes and effects) as may be requested by the DCC Security Trustee.

(ii) DCC shall discuss and agree with the DCC Security Trustee (the agreement of the DCC Security Trustee not to be unreasonably withheld or delayed) its plans for appropriate remedial action and the timetable for implementation of such action. The agreed remedial plan shall then be implemented by DCC.

3. **Independent Review**

(i) The DCC Security Trustee may, at its discretion, commission an independent review (the "**Independent Review**") to be undertaken on the timetable stipulated by the DCC Security Trustee. The Independent Review will be conducted by technical advisers to the DCC Security Trustee appointed from time to time or such other person as the DCC Security Trustee may decide.

(ii) The Independent Review shall examine the causes of the relevant Trigger Event and recommend appropriate corrective measures.

(iii) DCC shall cooperate 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.

4. **Consultation with Ofwat**

The DCC Security Trustee shall be entitled to discuss the relevant Trigger Event and the agreed remedial plan with Ofwat at any time.

5. **Appointment of Additional Non-executive Directors**

If the relevant Trigger Event has not otherwise been remedied or waived and:

(i) the agreed remedial plan has not been implemented to the reasonable satisfaction of the DCC Security Trustee within the agreed timetable;

(ii) any agreed remedial plan does not continue to be implemented to the reasonable satisfaction of the DCC Security Trustee; or

(iii) DCC and the DCC Security Trustee fail to agree on a remedial plan within the stipulated time limit,

the DCC Security Trustee shall be entitled to procure the appointment of additional non-executive directors to the board of DCC.

In respect of any of the Trigger Event Consequences described above which require the DCC Security Trustee to exercise its discretion, it shall do so upon instructions of the Beneficiary Instructing Group. The DCC Security Trustee is entitled to assume that no Trigger Event has occurred unless informed otherwise.

Trigger Event Remedies

At any time when DCC believes that a Trigger Event has been remedied by virtue of any of the following, it shall serve notice on the DCC Security Trustee to that effect, and the DCC Security Trustee shall respond within the agreed time limit 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 DCC Security Trustee is reasonably satisfied that the Trigger Event has been remedied).

The following shall constitute remedies to the Trigger Events:

1. **ICR and RAR**

The occurrence of a Trigger Event referred to in paragraph 1 of Trigger Events shall be remedied if, on any subsequent date:

(i) the ICR for the immediately preceding financial year is, and for each subsequent financial year until the next periodic review is projected to be, 2.0:1 or greater; and

(ii) the RAR for the immediately preceding financial year is, and for each subsequent financial year until the next periodic review is projected to be, 0.90:1 or less; and

(iii) the ICR for the immediately preceding financial year is, and for each subsequent financial year is projected to be, (adjusted to deduct actual or planned capital maintenance expenditure from the numerator) is greater than 1:1.

2. **Credit Rating Downgrade**

The occurrence of a Trigger Event referred to in paragraph 2 of Trigger Events shall be remedied if the credit rating of the relevant class of Bonds given by any two of the Rating Agencies is above the Trigger Credit Rating.

3. **Debt Service Payment Account Shortfall**

The occurrence of a Trigger Event referred to in paragraph 3 of Trigger Events shall be remedied if the credit balance of the Debt Service Payment Account is restored to the required level.

4. **Material Deviation in Projections**

The occurrence of a Trigger Event referred to in paragraph 4 of Trigger Events shall be remedied if the deviations referred to in that paragraph, on any subsequent date, are less than 10 per cent.

5. **Capex Reserve Shortfalls**

The occurrence of a Trigger Event referred to in paragraph 5 of Trigger Events shall be remedied on any subsequent date if the Capex Reserve Facility Amount is equal to or greater than the Net Capex Requirement for the twelve months immediately following the relevant Calculation Date.

6. **Drawdown on Liquidity Facility**

The occurrence of a Trigger Event referred to in paragraph 6 of Trigger Events shall be remedied if the drawing under the relevant Liquidity Facility is repaid in full without such repayment being funded by the making of any further drawing under that Liquidity Facility and that such Liquidity Facility or another Liquidity Facility is available for drawing in the future.

7. **Enforcement Orders**

The occurrence of a Trigger Event referred in paragraph 7 of Trigger Events shall be remedied if DCC has complied with the terms of the relevant Enforcement Order to the reasonable satisfaction of the DCC Security Trustee or if the Enforcement Order has been effectively withdrawn or if, in the opinion of the DCC Security Trustee (acting reasonably), the relevant fine will not have a Material Adverse Effect or that the Licence will not be terminated.

8. **Circumstances leading to a Special Administration Order**

The occurrence of a Trigger Event referred to in paragraph 8 of Trigger Events shall be remedied if (a) a special administration order is not made within six months of the relevant Trigger Event occurring or (b) the DCC Security Trustee is reasonably satisfied that a special administration order will not be made in respect of DCC.

9. **Termination of Licence**

The occurrence of a Trigger Event referred to in paragraph 9 of Trigger Events will be remedied by agreement by DCC of a transfer scheme which is reasonably satisfactory to the DCC Security Trustee.

10. **Event of Default**

The occurrence of a Trigger Event referred to in paragraph 10 of Trigger Events will be remedied upon the acceptance by the DCC Security Trustee of an agreed remedial plan and implementation of such plan has commenced to the reasonable satisfaction of the DCC Security Trustee.

11. **Material Entity Event**

The occurrence of a Trigger Event referred to in paragraph 11 of Trigger Events will be remedied upon the acceptance by the DCC Security Trustee of an agreed remedial plan and implementation of such plan has commenced to the reasonable satisfaction of the DCC Security Trustee.

In respect of any of the Trigger Event Remedies described above which require the DCC Security Trustee to exercise its discretion, it shall do so upon instructions of the Beneficiary Instructing Group, and any reference to reasonableness and reasonable time shall be interpreted accordingly.

DCC Events of Default

The Common Terms Agreement contains a number of events of default (the "**DCC Events of Default**"). Subject to agreed exceptions, materiality qualifications and grace periods, DCC Events of Default will include non-payment, misrepresentation, breach of covenant (including financial covenants and failure to comply with the Outsourcing Policy), default under DCC's own contracts, insolvency events (including special administration), insolvency proceedings (including the appointment of a special administrator), execution or distress, failure to comply with final judgment, a change of control of any Obligor, illegality, governmental intervention, litigation, change of business, termination of the Licence or, if a notice to terminate the Licence is served, the failure to implement an agreed transfer scheme at least two years prior to the termination date specified in such notice.

In respect of each DCC Event of Default requiring any action or discretion on the part of the relevant creditor, the relevant Security Trustee will act in accordance with the instructions of the Beneficiary Instructing Group or the Issuer Instructing Group in accordance with the DCC STID and the Issuer STID, respectively.

The occurrence of a DCC Event of Default will automatically give rise to a Standstill Event under the DCC STID (see "*DCC STID*" below).

Conditions Precedent

The conditions precedent to the entering into of the Common Terms Agreement by all the parties thereto will include:

- appropriate corporate resolutions, incumbency certificates, legal opinions and related documents;
- each of the DCC Transaction Documents duly signed by each party thereto; and
- no Potential Event of Default or Event of Default (however described) being continuing under any DCC Transaction Document.

DCC Deed of Charge

DCC will on or before the Initial Issue Date enter into a deed of charge (the "**DCC Deed of Charge**") with the DCC Security Trustee pursuant to which DCC will secure its obligations to the DCC Secured Creditors. The creation, perfection and enforcement of such security will each be subject to the WIA, the Licence and requirements thereunder. The DCC Deed of Charge will, to the extent applicable, incorporate the provisions of the Common Terms Agreement.

The security constituted by the DCC Deed of Charge (the "**DCC Security**") will be expressed to include:

- a first fixed charge over DCC's right, title and interest from time to time in and to:
    - any real property currently owned by DCC or acquired after the date of the DCC Deed of Charge;
    - the proceeds of disposal of any protected land;
    - any tangible moveable property;
    - DCC's Accounts;
    - any intellectual property rights owned by DCC;
    - any goodwill and rights in relation to the uncalled capital of DCC;
    - each investment of DCC's funds in certain eligible investments;
    - all shares of DCC in WWUF, all dividends, interest and other monies payable in respect thereof and all other rights related thereto;
- an assignment of DCC's right, title and interest from time to time in and to:
    - the proceeds of any insurance policies and all rights related thereto;
    - all rights and claims in relation to the DCC Accounts;
    - all contracts (subject to certain exceptions) with third parties (including each of the Contractors);
    - all monetary claims and all rights related thereto, including all accounts receivable (and to the extent that any accounts receivable cannot be effectively assigned as described, DCC shall hold the same on trust for the DCC Security Trustee absolutely);
    - the DCC Transaction Documents; and
- a first floating charge of the whole of the undertaking, property, assets and rights whatsoever and wheresoever present and future of DCC,

to the extent that, in all cases, such security is not created over protected land or would otherwise contravene the terms of the WIA, the Licence and requirements thereunder, or any other applicable statute or law.

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

For a description of certain limitations on the ability of DCC to grant security and certain limitations and restrictions on the security purported to be granted, see Chapter 8 under "*Security*". In addition, notice of the creation of the DCC Security will not be given initially to DCC's customers or to DCC's

contractual counterparties in respect of its contracts (other than certain material contracts). Each charge over DCC's land as purported to be granted will also take effect in equity only. Accordingly, until any such assignment is perfected, registration effected with HM Land Registry in respect of registered land or certain other action is taken in respect of unregistered land, any such assignment or charge may be or become subject to prior equities arising (such as rights of set-off).

Guarantor Security

On or before the Initial Issue Date, each of the Guarantors will enter into a guarantee and deed of charge (respectively, the "**Holdings Deed of Charge**", the "**HUH Deed of Charge**", the "**Glas Securities Deed of Charge**" and the "**Glas Deed of Charge**" and, together, the "**Deeds of Charge**") with the DCC Security Trustee, for itself and on behalf of the DCC Secured Creditors, pursuant to which each of them will guarantee to the DCC Security Trustee, for itself and on behalf of the DCC Secured Creditors, the obligations of DCC to the DCC Secured Creditors. The HUH Security (as defined below) will be released upon completion of the Share Purchase Agreement, and the Glas Security and the Glas Securities Security (each as defined below) will become effective from completion thereunder.

The guarantee from Holdings (the "**Holdings Guarantee**") will be secured by a first fixed charge over its shares in DCC and the Issuer, an assignment of its rights under the Holdings/DCC Loan Agreement and a first ranking floating charge over all the assets and undertaking of Holdings. The guarantee from HUH (the "**HUH Guarantee**") will be secured by a first fixed charge over its shares in Holdings and a "featherweight" floating charge over all the assets and undertaking of HUH. The guarantee from Glas Securities (the "**Glas Securities Guarantee**") will (subject to completion of the Share Purchase Agreement) replace the HUH Guarantee and will be secured by first fixed charges over its shares in Holdings and its rights under the Share Purchase Agreement and a first ranking floating charge over all the assets and undertaking of Glas Securities. The guarantee from Glas (the "**Glas Guarantee**" and, together with the Holdings Guarantee, the HUH Guarantee and the Glas Securities Guarantee, the "**Guarantees**") will be secured by a first fixed charge over its shares in Glas Securities and a first ranking floating charge over all the assets and undertaking of Glas.

Each of the Deeds of Charge will, to the extent applicable, incorporate the provisions of the Common Terms Agreement.

The Holdings Guarantee and the security constituted by the Holdings Deed of Charge (the "**Holdings Security**"), the HUH Guarantee and security constituted by the HUH Deed of Charge (the "**HUH Security**"), the Glas Securities Guarantee and security constituted by the Glas Securities Deed of Charge (the "**Glas Securities Security**") and the Glas Guarantee and security constituted by the Glas Deed of Charge (the "**Glas Security**" and, together with the Holdings Security, the HUH Security and the Glas Securities Security, the "**Guarantor Security**") will be held by the DCC Security Trustee for itself and on behalf of the DCC Secured Creditors in accordance with, and subject to, the terms of the DCC STID and will be enforceable if (a) the respective Guarantor defaults under its respective Deed of Charge which default or breach is not remedied, (b) such Guarantor breaches any of its covenants set out in the Common Terms Agreement which default or breach is not remedied or (c) a DCC Event of Default occurs. In addition, if a Guarantor (other than HUH) breaches any of its respective representations, warranties or covenants under the Common Terms Agreement and such breach is not remedied within any applicable grace period or if a Standstill occurs, such Guarantor will jointly and severally be obliged, together with each other Guarantor (other than HUH), to deposit in an account with the Account Bank in the name of the DCC Security Trustee by way of security for its guarantee obligations the aggregate principal amount outstanding under the Intercompany Loan Agreements.

None of Holdings, Glas Securities or Glas is expected to have any significant assets other than the shares in their respective subsidiaries.

DCC STID

Each of the DCC Security Trustee and the other DCC Secured Creditors, DCC, Holdings, HUH (until completion under the Share Purchase Agreement), Glas Securities, Glas the Issuer Security Trustee and the DCC Security Trustee will, on or before the Initial Issue Date, enter into the DCC STID pursuant to which, *inter alia*, the DCC Security Trustee will be appointed as trustee of the DCC Security, and of the Holdings Security, the HUH Security (until completion under the Share Purchase Agreement), the Glas Securities Security and the Glas Security (from completion under the Share Purchase Agreement). The DCC STID will regulate, *inter alia*, the rights of the DCC Secured Creditors

to require the DCC Security Trustee to enforce the DCC Security and the Guarantor Security and will set out the ranking in point of payment of the claims of the DCC Secured Creditors to the proceeds of such enforcement.

The DCC Security Trustee will act as trustee on behalf of the DCC Secured Creditors in connection with the DCC Security and the Guarantor Security. In such capacity, the DCC Security Trustee will agree that it will exercise any right which it may have in respect of the DCC Transaction Documents only as directed by the Beneficiary Instructing Group (subject to certain entrenched rights and reserved matters). See "*Intercreditor Arrangements*" above.

The DCC STID will provide that except with respect to any vote which would have the effect of terminating any Standstill (as to which, see "*Standstill*" below), the DCC Security Trustee will take action only when the instructions for or against such matter exceed 50 per cent. of the Qualified DCC Secured Liabilities. In each case, the DCC Security Trustee will not be liable to any person in relation to actions taken or not taken by it and will not be obliged to take action unless indemnified and/or secured to its satisfaction.

Entrenched Rights of DCC Secured Creditors

The rights of a Beneficiary Instructing Group to make decisions as to, *inter alia*, waivers of DCC Events of Default, modifications to DCC Transaction Documents and other issues potentially affecting the rights of one or more DCC Secured Creditors will be subject to certain entrenched rights of each DCC Secured Creditor. These entrenched rights cannot be changed without the consent of the relevant DCC Secured Creditors and include any:

- change to their ranking in priority as against other DCC Secured Creditors;
- change to the date fixed for payment of principal or interest under, or reduction in the amount of principal or interest payable on any date or any alteration in the method of calculating the amount or date of any payment under, any DCC Transaction Document;
- substitution of the principal obligor under any DCC Transaction Document;
- change in the currency of any payment due under a DCC Transaction Document; or
- modification of certain key terms in the DCC Transaction Documents.

Undertakings of DCC Secured Creditors

Pursuant to the terms of the DCC STID each DCC Secured Creditor (other than the DCC Security Trustee) will undertake that it will not, unless the Beneficiary Instructing Group otherwise agrees:

- permit or require any of DCC, Holdings, HUH (until completion under the Share Purchase Agreement), Glas Securities and Glas (each an "**Obligor**") to discharge any of the DCC Secured Liabilities (as defined in the Common Terms Agreement) owed to it save to the extent permitted by the Common Terms Agreement and the DCC STID;
- permit or require any Obligor to pay, prepay, redeem, purchase, early or voluntarily terminate or otherwise acquire any of the DCC Secured Liabilities owed to it save to the extent permitted by the Common Terms Agreement and the DCC STID;
- take, accept or receive the benefit of any security interest, guarantee, indemnity or other assurance against financial loss in respect of any of the DCC Secured Liabilities owed to it except the security interests under the DCC Security Documents or pursuant to the terms of the DCC Transaction Documents;
- take or receive from any of the Obligors by cash receipt, set-off or in any other manner whatsoever, the whole or any part of the DCC Secured Liabilities owed to it (save as permitted by the terms of the Common Terms Agreement and the DCC STID); or
- subject to agreed exceptions, agree to any amendment of the DCC Transaction Documents to which it is a party.

Undertakings of Obligors

Pursuant to the terms of the DCC STID, each Obligor will undertake that it will not, unless the Beneficiary Instructing Group otherwise agrees:

- discharge any of the DCC Secured Liabilities save to the extent permitted by the Common Terms Agreement and the DCC STID;

- pay, prepay, redeem, purchase, early or voluntarily terminate or otherwise acquire any of the DCC Secured Liabilities owed by it save to the extent permitted by the Common Terms Agreement and the DCC STID;
- 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 DCC Secured Liabilities owed by it except the security interests under or pursuant to the terms of the DCC Transaction Documents;
- discharge any of the DCC Secured Liabilities by set-off, any right of combination of accounts or otherwise (save as permitted by the terms of the Common Terms Agreement and the DCC STID);
- subject to agreed exceptions, agree to any amendment to the DCC Transaction Documents to which it is a party; or
- take or omit to take any action whereby any subordination contemplated by the DCC STID may be impaired.

Standstill

Immediately upon notification to the DCC Security Trustee of the occurrence of a DCC Event of Default under the Common Terms Agreement or the occurrence of any deferral of interest in respect of any Scheduled Interest Amount under any Advance of the proceeds of Class C Bonds under any Intercompany Loan Agreement (each such occurrence a "**Standstill Event**"), the DCC STID will provide for an automatic standstill of claims of the DCC Secured Creditors against DCC (the "**Standstill**"). The period of the Standstill (the "**Standstill Period**") will be the period from the date of such notification to the earlier of (i) except in the case of a Standstill Extension, the date on which a Beneficiary Instructing Group comprising more than $66\frac{2}{3}$ per cent. of the aggregate BIG Outstanding Principal Amount of the Qualified DCC Secured Liabilities elects to terminate the Standstill, (ii) the date on which a petition is presented for the special administration of DCC, (iii) the date on which the Standstill Event is remedied or waived, (iv) the date on which any acceleration of the Issuer Secured Liabilities occurs, and (v) in the case of a Standstill Extension, the date on which the relevant percentage of the aggregate BIG Outstanding Principal Amount of the Qualified DCC Secured Liabilities elects to terminate the Standstill.

During the Standstill Period:

- none of the DCC Secured Creditors will be entitled to accelerate any of the DCC Secured Liabilities or direct the DCC Security Trustee to take any steps to recover payment of any DCC Secured Liabilities from DCC or to enforce the DCC Security save to the extent permitted by the Common Terms Agreement and the DCC STID;
- the Guarantor Security will be enforceable at any time by the DCC Security Trustee at the direction of the Beneficiary Instructing Group; and
- the claims of the DCC Secured Creditors will be ranked in accordance with the DCC Standstill Priority (see "*DCC Cash Management*" below).

In the event that a Standstill Period has not been terminated prior to the date 18 months after the occurrence of the Standstill Event, on or before the last day of such 18 month period the Beneficiary Instructing Group will vote whether to terminate the Standstill Period. Unless the Beneficiary Instructing Group comprising those DCC Secured Creditors holding more than $66\frac{2}{3}$ per cent. of the DCC Secured Liabilties determines to terminate the Standstill Period, the Standstill Period will be extended (a "**Standstill Extension**") for a period of two months. On or before the last day of the Standstill Extension a further vote of the Beneficiary Instructing Group will be taken, provided that, for the purposes of such further vote (the "**Second Standstill Vote**"), the Beneficiary Instructing Group shall comprise those DCC Secured Creditors holding more than 50 per cent. of the DCC Secured Liabilities. Unless the Beneficiary Instructing Group determines to terminate the Standstill Period at the Second Standstill Vote, a Standstill Extension of another two months will occur. On or before the last day of the second Standstill Extension, a third vote (the "**Third Standstill Vote**") of the Beneficiary Instructing Group will be taken, provided that, for the purposes of such Third Standstill Vote, the Beneficiary Instructing Group shall comprise those DCC Secured Creditors holding more than $33\frac{1}{3}$ per cent. of the DCC Secured Liabilities. Unless the Beneficiary Instructing Group determines to terminate the Standstill Period at the Third Standstill Vote, a Standstill Extension of another two months will occur. On or before the last day of the third Standstill Extension, a fourth vote (the "**Fourth Standstill Vote**") of the

Beneficiary Instructing Group will be taken, provided that, for the purposes of such Fourth Standstill Vote, the Beneficiary Instructing Group shall comprise those DCC Secured Creditors holding more than 10 per cent. of the DCC Secured Liabilities. Unless the Beneficiary Instructing Group determines to terminate the Standstill Period at the Fourth Standstill Vote, a Standstill Extension of another six months will occur. On or before the last day of the Fourth Standstill Extension, a fifth vote (the "**Fifth Standstill Vote**") of the Beneficiary Instructing Group will be taken, provided that, for the purposes of such Fifth Standstill Vote, the Beneficiary Instructing Group shall comprise those DCC Secured Creditors holding more than 5 per cent. of the DCC Secured Liabilities. Unless the Beneficiary Instructing Group determines to terminate the Standstill at the Fifth Standstill Vote, the Standstill shall continue until the Beneficiary Instructing Group comprising DCC Secured Creditors comprising those DCC Secured Creditors holding more than 5 per cent. of the DCC Secured Liabilities determines to terminate the Standstill and a vote shall be taken on the expiry of each period of two months for so long as the Standstill continues. Accordingly, provided the thresholds above are met, the Standstill Period will terminate notwithstanding any votes to the contrary. Following termination of the Standstill Period, if a DCC Event of Default is still continuing, any DCC Secured Creditor may accelerate its DCC Secured Liabilities, at which point all other DCC Secured Liabilities will automatically accelerate, and the enforcement of the DCC Security and the Guarantor Security shall be undertaken by the DCC Security Trustee on behalf of the DCC Secured Creditors pursuant to the provisions of the DCC STID.

Standstill Cash Manager

Following the occurrence of a Standstill Event and for so long as a Standstill Period subsists, money credited to the Debt Service Payment Account will be applied by the Standstill Cash Manager in accordance with the DCC Standstill Priority (see "*DCC Standstill Priority*" below).

Enforcement

Subject to certain matters and with certain exceptions, following an enforcement, any proceeds of enforcement or other monies held by the DCC Security Trustee under the DCC STID will be applied by the DCC Security Trustee in accordance with the DCC Post-Enforcement Payments Priorities (see "*DCC Cash Management*" below).

Accession of Additional DCC Secured Creditors

The DCC STID requires that, to the extent that DCC wishes any Authorised Lender, further DCC Finance Lessor or other person to obtain the benefit of the DCC Security, such Authorised Lender, further DCC Finance Lessor or other person must sign an accession memorandum whereby it agrees to be bound by the terms of the DCC STID, including those provisions which prohibit individual DCC Secured Creditors from taking certain actions against DCC without the consent of the DCC Security Trustee and/or the Beneficiary Instructing Group. Such additional DCC Secured Creditor will also be required to accede to the terms of the Common Terms Agreement.

Master Framework Agreement

Introduction

The Issuer Security Trustee, for itself and on behalf of the Issuer Secured Creditors, the Cash Manager and the Issuer, will, on or before the Initial Issue Date, enter into a master framework agreement (the "**Master Framework Agreement**"). The Master Framework Agreement will set out the common terms, representations, warranties and covenants (positive, negative and financial) (collectively, the "**Issuer Common Terms**") which will, to the extent incorporated, apply to the Trust Deed, the Issuer Deed of Charge, the Liquidity Facility Agreements, the Hedging Agreements, the Paying Agency Agreement, the Issuer STID and certain other agreements between or in respect of the Issuer and the Issuer Secured Creditors. It will also contain the Issuer cash management provisions (see "*Issuer Cash Management*" below).

Issuer Warranties and Covenants

The Issuer will provide warranties and covenants standard for a special purpose vehicle of its sort issuing debt obligations such as the Bonds. The Issuer's warranties will include (i) corporate warranties in respect of its due incorporation, solvency and residency and in respect of there being no breaches of its general obligations, no litigation involving it or its assets, no outstanding consents required for its business and no involvement in business activities other than as permitted by the Issuer Transaction Documents (as defined below); and (ii) transaction warranties in respect of the due authorisation and

execution of the Issuer Transaction Documents, the due issuance of and the status and ranking of the Bonds, the accuracy of the information contained in this Information Memorandum and the absence of any outstanding consents or breaches of its obligations in respect of the Bonds.

The Issuer's covenants will include (i) corporate covenants to prepare audited financial statements, to conduct its business in accordance with applicable law, to obtain all necessary consents and, other than as permitted by or pursuant to the Issuer Transaction Documents, not to carry on any business, incur any indebtedness, permit to exist or create any security, make any loans, merge or consolidate with any other entity or amend its constitutional documents or any of the agreements to which it is party; (ii) transaction covenants to comply with all its obligations under the Issuer Transaction Documents, to preserve all its rights thereunder, to provide the Issuer Secured Creditors with all necessary information and to notify the relevant parties of any Issuer Event of Default or potential Issuer Event of Default; (iii) asset covenants to maintain proper books and records in respect of its assets, to protect all its rights in respect thereof and to take all such further actions as may be necessary to preserve its assets; and (iv) bond covenants to obtain and maintain the listings of the Bonds, to provide all notices under the Conditions (including to the Bondholders, the Paying Agents, the Transfer Agents, the Registrar and the Rating Agencies) and to notify the appropriate parties of potential late payments or any proposed early redemptions of any of the Bonds.

Issuer Events of Default

The Issuer Events of Default are set out in Condition 11(a) in Chapter 6 under "*Terms and Conditions of the Bonds*".

The Issuer Deed of Charge

The Issuer will, on or before the Initial Issue Date, enter into the Issuer Deed of Charge with the Issuer Security Trustee (for itself and on behalf of the Bond Trustee (for itself and on behalf of the Bondholders), the Financial Guarantors, the Liquidity Facility Providers, the Hedge Counterparties, the Account Bank, the Authorised Lenders, the Registrar, the Transfer Agents, the Paying Agents, the Agent Bank, the Cash Manager, any receiver and any other creditor of the Issuer which accedes to the Issuer STID (together the "**Issuer Secured Creditors**")). Pursuant to the Issuer Deed of Charge, the Issuer will secure its obligations to the Issuer Secured Creditors by granting the following security:

- a first fixed sub-charge of the benefit of the Issuer's interest in and to the DCC STID;
- a first fixed charge of each investment of the Issuer's funds in certain eligible investments;
- a first fixed charge of the benefit of the Issuer Accounts and any bank or other accounts in which the Issuer may at any time have or acquire any benefit;
- an assignment of the benefit of each Issuer Transaction Document; and
- a first floating charge of the whole of the undertaking, property, assets and rights whatsoever and wheresoever present and future of the Issuer,

such security expressly to exclude all moneys constituting the issued share capital of the Issuer not otherwise utilised by the Issuer from time to time and the corporate benefits fee of £1,000 payable by DCC to the Issuer on the Initial Issue Date.

The Issuer Deed of Charge will, to the extent applicable, incorporate the Issuer Common Terms as set out in the Master Framework Agreement.

The Issuer Security will be held on trust by the Issuer Security Trustee for itself and on behalf of the Issuer Secured Creditors in accordance with, and subject to, the Issuer Deed of Charge and the Issuer STID.

Issuer STID

The Issuer, the Issuer Security Trustee, the Bond Trustee (for itself and on behalf of the Bondholders), MBIA, the Initial Liquidity Provider, the Initial Hedge Counterparties, the Initial Authorised Lender, the Account Bank, the Principal Paying Agent, the Paying Agent, the Cash Manager, the Agent Bank, the Registrar and the Transfer Agent will, on or before the Initial Issue Date, enter into the Issuer STID. Under the Issuer STID, the Issuer Security Trustee will be appointed as trustee for the Issuer Secured Creditors and the parties will agree to certain intercreditor arrangements. The composition of the Issuer Instructing Group through which instructions will be given to the Issuer Security Trustee in respect of, *inter alia*, the exercise of any rights of the Issuer under the DCC

Transaction Documents or the enforcement of the DCC Security or the Guarantor Security or the giving of any consent or the making of any amendments has been described previously (see "*Intercreditor Arrangements*" above).

Entrenched Rights of Issuer Secured Creditors

The rights of an Issuer Instructing Group to make decisions as to matters potentially affecting the rights of one or more Issuer Secured Creditors will be subject to certain entrenched rights of each Issuer Secured Creditor. The specific entrenched rights of each of the Issuer Secured Creditors are intended to ensure that an Issuer Secured Creditor's consent will be required to any action which would materially adversely affect such Issuer Secured Creditor's rights, including any:

- change to their ranking in priority as against other Issuer Secured Creditors;
- change to the date fixed for payment of principal or interest under, or reduction in the amount of principal or interest payable on any date or any alteration in the method of calculating the amount or date of any payment under, any Issuer Transaction Document;
- change in the currency of any payment due under an Issuer Transaction Document;
- modification of certain key terms in the Issuer Transaction Documents; or
- modifications causing a rating downgrade below the original ratings of the Bonds (other than the Class D Bonds).

Exercise of Rights by Bond Trustee

When exercising any rights, powers, trusts, authorities and discretions relating to or contained in the Conditions or the Trust Deed (other than in respect of any Entrenched Right or Reserved Matter or Basic Terms Modification, or determining the occurrence of an Entrenched Right, Reserved Matter or Basic Terms Modification) which affects or relates to any Class A Bonds, the Bond Trustee shall only act with the consent of the Issuer Instructing Group (unless the Bond Trustee is the Issuer Instructing Group) or subject to any Reserved Matter in accordance with the provisions of the Issuer STID, 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 (see Condition 16(b) in Chapter 6 under "*Terms and Conditions of the Bonds*").

The Financial Guarantor of the first Series of Class A Bonds will have additional entrenched rights so as to ensure, *inter alia*, that certain core covenants of DCC regarding its business activities and operations and certain key financial ratios contained in the Common Terms Agreement cannot be changed or waived without the prior consent of that Financial Guarantor.

Acknowledgement Regarding Issuer Transaction Documents

Each Issuer Secured Creditor which signs the Issuer STID as at the Initial Issue Date (a) agrees to be bound by the terms of the Issuer STID, including the intercreditor arrangements, and (b) will be deemed to have knowledge of, and will be bound by, the terms of all the Issuer Transaction Documents.

Actions Requiring Consent

The consent of the Issuer Security Trustee (acting on instructions from the Issuer Instructing Group) will be required, *inter alia*:

- for any modification (i.e., waiver, variation or amendment) of any of the Issuer Transaction Documents, or any exercise of any right, power or discretion thereunder (other than modifications of a minor or technical nature);
- for any release of or impairment to any part of the Issuer Security except as expressly permitted by the Issuer Transaction Documents; and
- for any action (including the withdrawal of most sums from any of the Issuer Accounts) following an event of default under the Issuer Transaction Documents which remains unremedied and unwaived.

Accession of Additional Issuer Secured Creditors

The Issuer Deed of Charge and the Issuer STID require that, to the extent that the Issuer wishes any additional creditor to obtain the benefit of the Issuer Security, such creditor must sign an accession memorandum whereby it (a) agrees to be bound by the terms of the Issuer STID, including the intercreditor arrangements, and (b) will be deemed to have knowledge of, and will be bound by, the terms of all the Issuer Transaction Documents.

If the Issuer wishes to raise additional financing through the issue of further Bonds under the Programme or through Authorised Loan Facilities or otherwise, it may only do so provided that the DCC financial covenants set out in the Common Terms Agreement (see "*Common Terms Agreement*" above) are not breached as a result of the Issuer making a corresponding advance under an Intercompany Loan Agreement with the proceeds of such additional financing.

Financial Guarantor Documents

The Bond Policies

The form of Bond Policies to be issued by MBIA (upon fulfilment or waiver by MBIA of certain conditions precedent to be contained in the relevant I&I Agreement) in respect of the issue of Class A Bonds to be issued on the Initial Issue Date is set out in full in Chapter 7 under "*MBIA Bond Policy*". To the extent that any other Financial Guarantors issue Bond Policies in respect of any further Series of Class A Bonds, such Bond Policies are expected to be issued by such Financial Guarantor(s) on terms substantially similar thereto.

On or before the Initial Issue Date, MBIA will issue in favour of the Bond Trustee (for itself and on behalf of the relevant Class A Bondholders) a Bond Policy for each Sub-Class of the Class A Bonds issued on the Initial Issue Date in respect of scheduled interest (other than any Subordinated Coupon Amounts) and principal (other than any accelerated amounts) on the relevant Sub-Class of Class A Bonds (see Chapter 7 under "*Form of Bond Policy*").

Upon an early redemption of the relevant Class A Bonds or an acceleration of the relevant Class A 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 Policies) on each Issuer 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, but only after an acceleration of the Bonds, 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 Class A Bonds together with accrued interest. Any amounts due in excess of such outstanding principal amount (and any accrued interest thereon) and any Subordinated Coupon Amounts 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 to be issued by MBIA on the Initial Issue Date 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.

Insurance and Indemnity Agreements

On each relevant Issue Date, the Issuer 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 any reasonable 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 Class A Bondholders against the Issuer in respect of any payments made.

DCC CASH MANAGEMENT

In this section:

any reference to a "**month**" is a reference to an accounting month of DCC;

"**New Money Advance**" means any drawing during a Standstill under the Tranche R1 or Tranche R2 of any Intercompany Loan Agreement or any Authorised Loan Agreement provided to DCC which is not made (or to the extent not made) for the purpose of refinancing a maturing R1 Advance or R2 Advance or refinancing a drawing under such Authorised Loan Agreement;

“**Relevant Series Proportion**” means the proportion represented by the fraction the numerator of which is the Principal Amount Outstanding of all Bonds issued under the relevant Series and the denominator of which is the Principal Amount Outstanding of all Bonds issued under all Series;

“**Subordinated Authorised Loan Amounts**” means, in relation to any Authorised Loan Agreement, the aggregate of any amounts payable by the Issuer to such Authorised Lender in respect of its obligation to gross up any payments made by it in respect of such Authorised Loan Agreement or to make any payment of increased costs to such Authorised Lender;

“**Subordinated Commissions**” means:

- in respect of any R Tranche, any amounts by which the commitment commissions on the undrawn portion of such R Tranche exceed the initial commitment commissions on the undrawn portion of such R Tranche as at the date on which the R Tranche was first made available; and

- in respect of any Class R Bonds, any amounts by which the underwriting commissions on the Class R Bonds exceed the initial underwriting commissions on the Class R Bonds as at the date on which the Class R Bonds were first issued;

“**Subordinated Coupon Amounts**” means, in respect of any Sub-Class of Bonds, any amounts (other than deferred interest) by which the Coupon on such Sub-Class exceeds the initial Coupon on such Sub-Class of Bonds as at the date on which such Sub-Class of Bonds was issued;

“**Subordinated Interest**” means, in respect of any Term Advances or Revolving Advances under any Intercompany Loan Agreement, any amounts by which the applicable margin on such Term Advances or Revolving Advances exceed the initial applicable margin on such Term Advances or Revolving Advances as at the date that such Intercompany Loan Agreement was first entered into; and

“**Subordinated Liquidity Facility Amounts**” has the meaning given to it in the section below entitled “*The Liquidity Facilities*”.

DCC’s Accounts and Ledgers

DCC has established or will, on or before the Initial Issue Date, establish the following bank accounts with the Account Bank: a receipts account (the “**Receipts Account**”), a payments account (the “**Payments Account**”), a debt service payment account (the “**Debt Service Payment Account**”), a reserves account (the “**Reserves Account**”), a customer payments account (the “**Customer Payments Account**”) and a rejected direct debits account (the “**RDD Account**”). DCC may not establish any further bank accounts unless it has first met certain conditions in respect thereof, which will be as set out in the Common Terms Agreement (including that such further accounts are (a) required for the operation of DCC’s Permitted Business, (b) the subject of a first fixed security under the DCC Deed of Charge and (c) are opened and maintained with a bank that has the Requisite Ratings). These accounts will include foreign currency accounts for the purpose of clearing payments to suppliers in foreign currencies, a customer compensation account for the purpose of funding minor compensation payments to customers and a treasury account for pooling certain credit balances for cash management purposes.

The Receipts Account, the Payments Account, the Debt Service Payment Account, the Reserves Account, the Customer Payments Account, the RDD Account and each other permitted bank account of DCC from time to time are collectively referred to as “**DCC’s Accounts**”. DCC’s Accounts will be held with the Account Bank pursuant to an account agreement (the “**DCC Account Bank Agreement**”) dated on or about the Initial Issue Date between DCC, the Account Bank and the DCC Security Trustee.

Receipts Account

Under the Common Terms Agreement, DCC will covenant in favour of the DCC Security Trustee that all of DCC’s revenues will be paid directly into the Receipts Account or be directed to be paid into the Payments Account. Monies credited from time to time to the Receipts Account will be transferred periodically at the discretion of DCC to the Payments Account or to the RDD Account (as described below) but not otherwise. On any Business Day (as defined in the Common Terms Agreement) DCC may direct that an amount equal to the aggregate amount of rejected direct debits from customers for any period as determined by DCC may be transferred from the Receipts Account to the RDD Account.

Payments Account

The Payments Account will be the current account of DCC through which all sterling denominated operating and capital expenditure of DCC will be cleared. Operating expenditure (including payments to Contractors and to WPD Finance under the CfD) will be funded by cash transfers from the Receipts Account and through drawings, as and when required, under an overdraft facility in the amount of £20,000,000 to be provided by the Overdraft Bank on or before the Initial Issue Date (the ''**Overdraft Facility**'') and, if applicable, drawings under the Tranche R2 Facility or a DCC Authorised Loan Facility. Capital expenditure will be funded from available cashflow and cash transfers made during the course of each month from the Reserves Account. On the Initial Issue Date, out of the proceeds of drawdown of the Initial Term Advances, an amount equal to £34,000,000 will be paid into the Payments Account.

Under the Common Terms Agreement, DCC will covenant in favour of the DCC Security Trustee that on the opening of business on the first Business Day of each month an amount equal to $^{1}/_{12}$th (or, in the case of the first Relevant Year, $^{1}/_{10}$th) of DCC's Annual Finance Charge for the time being will be transferred from the Payments Account to the Debt Service Payment Account and credited to the Debt Service Ledger.

DCC's ''**Annual Finance Charge**'' shall be calculated by DCC on the Initial Issue Date and annually thereafter on 31 March of each year (or, if such day is not a Business Day, the immediately preceding Business Day) to be the sum of the following payments scheduled (or, where uncertain, estimated by DCC in good faith) to fall due and payable in (for the period from the Initial Issue Date to 31 March 2002) that period and (for any other period) in or (in the case of the DCC Finance Leases) upon or immediately following the expiry of the twelve month period commencing on 1 April of that year and ending on 31 March of the following year (each such period, a ''**Relevant Year**''):

(i) the aggregate amount of interest due on each outstanding Advance under the Intercompany Loan Agreements;

(ii) (except for the first Relevant Year) the aggregate amount of rental payments due to the DCC Finance Lessors under the DCC Finance Leases inclusive of any VAT (after (a) deducting any amount representing a repayment of capital under the DCC Finance Leases and any estimated rental rebates (inclusive of any VAT) and (b) adding back any further rentals due (inclusive of any VAT), in each case, as determined by DCC in good faith);

(iii) the aggregate amount of fees and commissions due to the Issuer under each Intercompany Loan Agreement; and

(iv) the aggregate amount of interest, fees and commissions due during the Relevant Year under any Authorised Loan Agreement provided to DCC.

DCC's Annual Finance Charge shall be adjusted during the course of a Relevant Year, upwards or downwards, as appropriate, to ensure that the annual amount reserved for within the Debt Service Payment Account will always be sufficient to meet in full the liabilities described above in any Relevant Year if, for any reason, any of those liabilities are modified (including as a result of any deferral) pursuant to, and as permitted by, the terms of the DCC Transaction Documents.

DCC's Annual Finance Charge shall additionally be increased to cover the aggregate amount of interest due to the Issuer in respect of any Revolving Advances made during a Relevant Year and to any Authorised Lender in respect of any drawings made by DCC under any Authorised Loan Agreement during a Relevant Year.

Reserves Account

On the Initial Issue Date, out of the proceeds of drawdown of the Initial Term Advances, an amount equal to £165,000,000 will be paid into the Reserves Account.

No monies may be withdrawn from the Reserves Account except for the purpose of any transfer to the Payments Account on account of DCC's forecast capital expenditure for the month in which such transfer occurs. Except for reconciliation payments made pursuant to the arrangements referred to below, in no circumstances shall DCC transfer in any month any monies from the Reserves Account to the Payments Account in excess of DCC's forecast capital expenditure for that month.

By no later than the last Business Day of each month DCC will reconcile, by reference to the management accounts prepared for the preceding month, the actual amount of capital expenditure incurred in the preceding month against the aggregate amount transferred during the preceding month from the Reserves Account on account of forecast capital expenditure for such preceding month. In the event that actual capital expenditure incurred in any preceding month exceeded the

amount transferred on account of forecast capital expenditure, the amount required to be transferred to the Payments Account in respect of forecast capital expenditure for the month following the month in which such management accounts have been prepared shall be increased by the amount of such excess less any amounts arising from DCC's operating cashflows applied in payment of such actual capital expenditure. In the event that actual capital expenditure incurred was less than the amount transferred on account of forecast capital expenditure, an amount equal to the difference shall be transferred forthwith from the Payments Account to the Reserves Account or, alternatively, at DCC's discretion, netted against amounts required to be transferred from the Reserves Account to the Payments Account on account of forecast capital expenditure in the month following the month in which such management accounts have been prepared.

DCC is not required to maintain any minimum credit balance on the Reserves Account. However, it may be a condition precedent to the making of any further Term Advances under any further Intercompany Loan Agreement, that DCC pays into the Reserves Account a specified portion of such further Term Advances. Furthermore, DCC will covenant in favour of the DCC Security Trustee in the Common Terms Agreement that on each Calculation Date the aggregate of (a) the amount credited to the Reserves Account and (b) the aggregate undrawn commitment under the Tranche R2 Facility under the Intercompany Loan Agreements and any replacement or supplemental facility provided for capital expenditure will be at least equal to the Net Capex Requirement for the following twelve months.

Debt Service Payment Account

DCC shall initially open and maintain in its books two ledgers in respect of the Debt Service Payment Account (respectively the "**Lease Payments Ledger**" and the "**Debt Service Ledger**").

Lease Payments Ledger

On the Initial Issue Date, out of the proceeds of drawdown of the Initial Term Advances, an amount equal to £12,000,000, representing aggregate scheduled annual payments due (inclusive of VAT) under the Finance Leases on 1 April 2002 (taking into account estimated rental rebates (inclusive of VAT) for that period as determined by DCC in good faith), will be paid into the Debt Service Payment Account and credited to the Lease Payments Ledger.

No monies may be withdrawn from the Debt Service Payment Account in respect of monies credited to the Lease Payments Ledger save to the extent required to meet scheduled rental payments (inclusive of any VAT) under the DCC Finance Leases falling on 1 April 2002.

Debt Service Ledger

Prior to the occurrence of a Standstill, monies credited to the Debt Service Ledger shall be applied by DCC only for the purpose of making the following payments ("**DCC Payments**") as and when the same fall due for payment:

- to the Issuer, in or towards satisfaction of any scheduled fees and interest due under each Tranche of each Intercompany Loan Agreement;
- to the DCC Security Trustee, in or towards satisfaction of any scheduled fees due to the DCC Security Trustee under the terms of the DCC STID;
- to the Standstill Cash Manager, in or towards satisfaction of any scheduled fees due to the Standstill Cash Manager;
- (except for the scheduled rental payments falling due in March and April 2002 where such payments will be met from amounts credited to the Lease Payments Ledger) to the DCC Finance Lessors, in or towards satisfaction of any scheduled rental payments (inclusive of VAT) due to the DCC Finance Lessors under the DCC Finance Leases (except for any capital repayments); and
- to any DCC Hedge Counterparty under any Permitted Treasury Transaction, in or towards satisfaction of any scheduled sums due to such DCC Hedge Counterparty under such Permitted Treasury Transaction.

Interest charges under the Overdraft Facility, repayment of the principal debit balance under the Overdraft Facility and any payments due under the CfD will be paid as and when the same fall due and payable out of sums paid into the Payments Account from the Receipts Account and/or the Customer Payments Account for the purpose of meeting operating expenditure.

For so long as a Standstill Event has not occurred, DCC shall, on the date which is five Business Days prior to each DCC Payment Date, determine whether the aggregate amount of monies then credited is at least equal to the DCC Payments falling to be paid on such DCC Payment Date. If there is an insufficiency of funds, then DCC shall promptly request from the Issuer the making of a Tranche L advance in an amount equal to the shortfall, such amount to be paid to DCC no later than the relevant DCC Payment Date.

Customer Payments Account

DCC shall initially open and maintain in its books two ledgers in respect of the Customer Payments Accounts (respectively, the "**General Ledger**" and the "**Customer Rebate Ledger**").

DCC may on the close of business of the last Business Day of each month transfer Available Monies from the Payments Account to the Customer Payments Account for the credit of the General Ledger provided that:

- the backward-looking and forward-looking ICR is greater than or equal to 2.0:1; and
- the RAR is less than or equal to 0.90:1.

"**Available Monies**" means the amount credited to the Payments Account as at the close of business on the last Business Day of each month after deducting the amount required to be transferred on the next following Business Day to the Debt Service Payment Account.

Rebates to customers may only be granted to the extent of monies credited to the General Ledger subject always to satisfaction of the conditions for the making of a Restricted Payment as set out in the Common Terms Agreement and provided further that the Customer Rebate Ledger is then credited with an amount equal to the aggregate amount of the relevant rebate. An amount equal to $^{1}/_{12}$th of the aggregate amount of rebates declared by DCC in respect of any Relevant Year shall be transferred from the Customer Payments Account to the Payments Account on the first Business Day of each month of the Relevant Year in which such rebate is to apply.

Monies credited to the Customer Payments Account will constitute the only source of funds available to DCC to make Restricted Payments.

DCC will be entitled to invest monies credited to DCC's Accounts in certain eligible investments and may for cash management purposes pool credit balances on all of DCC's Accounts (excluding the Debt Service Payment Account) through a separate investment account.

The cash management arrangements described above shall continue to apply until the occurrence of a Standstill Event. In the event of a Standstill occurring and during the period it is continuing, the arrangements described above shall be modified as follows:

- DCC's Annual Finance Charge shall be adjusted upwards to include the cost of any Tranche L Advances made under any Intercompany Loan Agreement and any payments to be made by DCC under the CfD;
- an amount equal to the aggregate sum credited to the Customer Payments Account shall be forthwith transferred to the Debt Service Payment Account;
- no payments may be made to WPD Finance under the CfD except out of sums credited to the Debt Service Payment Account and then only to the extent that such sums are available for that purpose in accordance with the priority described below (the "**DCC Standstill Priority**"); and
- the claims ("**Claims**") of the DCC Security Trustee, the Account Bank, the Standstill Cash Manager, the Issuer, the DCC Finance Lessors, each Authorised Lender, the Existing DCC Hedge Counterparty, each other party that enters a DCC Hedge Document, as defined in the DCC STID (each a "**DCC Hedging Counterparty**"), WPD Finance, any receiver of the Guarantors and any other creditor of DCC which accedes to the DCC STID (together the "**Standstill Creditors**") against DCC in respect of each Relevant Year shall be ranked in point of priority strictly in accordance with the order of priority as set out immediately below under the heading "*DCC Standstill Priority*".

DCC Standstill Priority

The DCC Standstill Priority is as follows:

(i) first, *pro rata* according to the respective amounts thereof, (a) the DCC Security Trustee in respect of the fees or other remuneration and indemnity payments (if any) payable to the DCC Security Trustee in respect of such Relevant Year and any costs, charges, liabilities and expenses incurred by the DCC Security Trustee under the DCC STID and the DCC Security Documents; and (b) any receiver of any Guarantor appointed under the Security Documents in respect of the fees or other remuneration and indemnity payments (if any) payable to such receiver in respect of such Relevant Year (such claims of the DCC Security Trustee and any receiver (and any such claims arising on any acceleration of liabilities against DCC under the DCC STID), a "**Tier 1 Claim**");

(ii) second, *pro rata* according to the respective amounts thereof, (a) the Issuer in respect of scheduled fees (other than commitment fees under Tranche R) due in respect of such Relevant Year under the Intercompany Loan Agreements and indemnity payments (if any) payable to the Issuer (in relation to any costs, charges, liabilities and expenses incurred by the Bond Trustee or the Issuer Security Trustee under the Issuer Transaction Documents in respect of such Relevant Year) under the Intercompany Loan Agreements and (b) the Standstill Cash Manager in respect of fees or remuneration due to the Standstill Cash Manager (such claims of the Issuer and the Standstill Cash Manager (and any such claims arising on any acceleration of liabilities against DCC under the DCC STID), a "**Tier 2 Claim**");

(iii) third, *pro rata* according to the respective amounts thereof:

(a) the Issuer in respect of:

(1) any Additional Amounts due in respect of such Relevant Year under the Intercompany Loan Agreements and any interest due in respect of the Relevant Year under any Tranche L Advances; and

(2) any interest and principal due in respect of such Relevant Year under any New Money Advances; and

(b) each Authorised Lender in respect of any interest and principal due in respect of such Relevant Year under any New Money Advances,

(such claims of the Issuer and such Authorised Lender (and any such claims arising on any acceleration of liabilities against DCC under the DCC STID), a "**Tier 3 Claim**");

(iv) fourth, *pro rata* according to the respective amounts thereof:

(a) each DCC Hedging Counterparty under a Permitted Treasury Transaction, in respect of payments to be made or any other sums due and payable in such Relevant Year under any interest rate hedging agreement (excluding any termination payment arising as a result of a default by such DCC Hedging Counterparty);

(b) the Issuer in respect of:

(1) interest due on any Tranche A Advances in respect of such Relevant Year (excluding any Subordinated Interest);

(2) interest due on any Tranche B Advances in respect of such Relevant Year (excluding any Subordinated Interest);

(3) interest due on any Revolving Advances in respect of such Relevant Year (excluding any Subordinated Interest and under any Tranche L Advances); and

(4) commitment fees on the R Advances in respect of such Relevant Year (excluding any Subordinated Commissions);

(c) each DCC Finance Lessor in respect of payments due in respect of such Relevant Year under the DCC Finance Leases (excluding any capital repayments or indemnity payments),

(such claims of each Hedging Counterparty, the Issuer and each DCC Finance Lessor (and any such claims arising on any acceleration of liabilities against DCC under the DCC STID), a "**Tier 4 Claim**");

(v) fifth, *pro rata* according to the respective amounts thereof:

(a) the Issuer in respect of:

(1) any principal repayment on any Tranche A Advances in respect of such Relevant Year;

(2) any principal repayment on any Tranche B Advances in respect of such Relevant Year; and

(3) any principal repayment on any Revolving Advances in respect of such Relevant Year (excluding, for this purpose, any principal repayment to be applied by the Issuer in making a further Tranche R Advance);

(b) each DCC Finance Lessor, in respect of any capital repayment due in respect of such Relevant Year under the relevant DCC Finance Lease,

(such claims of the Issuer and each DCC Finance Lessor (and any such claims arising on any acceleration of liabilities against DCC under the DCC STID), a "**Tier 5 Claim**");

(vi) sixth, the Issuer in respect of interest due in respect of such Relevant Year under the Tranche C Advances (such claims of the Issuer (and any such claims arising on any acceleration of liabilities against DCC under the DCC STID), a "**Tier 6 Claim**");

(vii) seventh, the Issuer in respect of any principal repayments due in respect of such Relevant Year under the Tranche C Advances (such claims of the Issuer (and any such claims arising on any acceleration of liabilities against DCC under the DCC STID), a "**Tier 7 Claim**");

(viii) eighth, the Issuer in respect of interest due in respect of the Relevant Year under the Tranche D Advances (such claims of the Issuer (and any such claims arising on any acceleration of liabilities against DCC under the DCC STID), a "**Tier 8 Claim**");

(ix) ninth, the Issuer in respect of any principal repayments due in respect of such Relevant Year under the Tranche D Advances (such claims of the Issuer (and any such claims arising on any acceleration of liabilities against DCC under the DCC STID), a "**Tier 9 Claim**");

(x) tenth, *pro rata* according to the respective amounts thereof:

(a) the DCC Finance Lessors in respect of any other amounts due to them under the DCC Finance Leases in respect of such Relevant Year;

(b) the Issuer in respect of any other sums due to the Issuer in respect of such Relevant Year (excluding Subordinated Interest);

(c) each Authorised Lender in respect of any other sums due in respect of such Relevant Year to such Authorised Lender; and

(d) each DCC Hedging Counterparty under a Permitted Treasury Transaction in respect of any termination payment due to such DCC Hedging Counterparty arising as a result of a default by such DCC Hedging Counterparty,

(such claims of the DCC Finance Lessors, the Issuer, each Authorised Lender and each DCC Hedging Counterparty (and any such claims arising on any acceleration of liabilities against DCC under the DCC STID), a "**Tier 10 Claim**");

(xi) eleventh, WPD Finance, in respect of any sums due in respect of such Relevant Year from DCC under the CfD (such claims of WPD Finance (and any such claims arising on any acceleration of liabilities against DCC under the DCC STID), a "**Tier 11 Claim**");

(xii) twelfth, the Issuer in respect of any Subordinated Interest due in respect of such Relevant Year under any Tranche A Advances, Tranche B Advances and Tranche R Advances *pro rata* to the respective amounts thereof (such claims of the Issuer (and any such claims arising on any acceleration of liabilities against DCC under the DCC STID), a "**Tier 12 Claim**");

(xiii) thirteenth, the Issuer in respect of any Subordinated Interest due in respect of such Relevant Year under any Tranche C Advance (such claims of the Issuer (and any such claims arising on any acceleration of liabilities against DCC under the DCC STID), a "**Tier 13 Claim**"); and

(xiv) fourteenth, the Issuer in respect of any Subordinated Interest due in respect of such Relevant Year under any Tranche D Advance (such claims of the Issuer (and any such claims arising on any acceleration of liabilities against DCC under the DCC STID), a "**Tier 14 Claim**").

To the extent there arises any requirement to gross up any payment under the Intercompany Loan Agreements or Authorised Loan Facilities made available to DCC, the payment in respect of such requirement will rank *pari passu* with the primary payment obligation which gave rise thereto.

Upon the occurrence of the Standstill, the Standstill Cash Manager on behalf of the DCC Security Trustee shall open and maintain the following ledgers ("**Standstill Ledgers**") in respect of the Debt Service Payment Account:

(i) a ledger ("**Tier 1 Ledger**") in respect of Tier 1 Claims which shall be divided into separate sub-ledgers for each person holding a Tier 1 Claim (such person a "**Tier 1 Creditor**");

(ii) a ledger ("**Tier 2 Ledger**") which shall be divided into separate sub-ledgers ("**Tier 2 Sub-Ledgers**") for each person holding a Tier 2 Claim (such person a "**Tier 2 Creditor**");

(iii) a ledger ("**Tier 3 Ledger**") which shall be divided into separate sub-ledgers ("**Tier 3 Sub-Ledgers**") for each person holding a Tier 3 Claim (such person a "**Tier 3 Creditor**") and, in the case of the Issuer, shall be further divided into sub-sub ledgers ("**Tier 3 Sub-Sub Ledgers**") in respect of each separate Tier 3 Claim of the Issuer;

(iv) a ledger ("**Tier 4 Ledger**") which shall be divided into separate sub-ledgers ("**Tier 4 Sub-Ledgers**") for each person holding a Tier 4 Claim (such person a "**Tier 4 Creditor**") and, in the case of the Issuer, shall be further divided into further sub-sub ledgers ("**Tier 4 Sub-Sub Ledgers**") in respect of each separate Tier 4 Claim of the Issuer;

(v) a ledger ("**Tier 5 Ledger**") which shall be divided into separate sub-ledgers ("**Tier 5 Sub-Ledgers**") for each person holding a Tier 5 Claim (such person a "**Tier 5 Creditor**") and, in the case of the Issuer, shall be further divided into further sub-sub ledgers ("**Tier 5 Sub-Sub Ledgers**") in respect of each separate Tier 5 Claim of the Issuer;

(vi) a ledger ("**Tier 6 Ledger**") in respect of the Issuer's Tier 6 Claim;

(vii) a ledger ("**Tier 7 Ledger**") in respect of the Issuer's Tier 7 Claim;

(viii) a ledger ("**Tier 8 Ledger**") in respect of the Issuer's Tier 8 Claim;

(ix) a ledger ("**Tier 9 Ledger**") in respect of the Issuer's Tier 9 Claim;

(x) a ledger ("**Tier 10 Ledger**") which shall be divided into separate sub-ledgers ("**Tier 10 Sub-Ledgers**") for each person holding a Tier 10 Claim (such person a "**Tier 10 Creditor**");

(xi) a ledger ("**Tier 11 Ledger**") in respect of WPD Finance's Tier 11 Claim;

(xii) a ledger ("**Tier 12 Ledger**") which shall be sub-divided into separate sub-ledgers ("**Tier 12 Sub-Ledgers**") in respect of each separate Tier 12 Claim of the Issuer;

(xiii) a ledger ("**Tier 13 Ledger**") in respect of the Issuer's Tier 13 Claim; and

(xiv) a ledger ("**Tier 14 Ledger**") in respect of the Issuer's Tier 14 Claim.

Subject to the entrenched rights of the Issuer Security Trustee and the other Issuer Secured Creditors (including the Bond Trustee), the terms of the DCC Standstill Priority may change if the Issuer issues a further Series of Bonds or enters into further Authorised Loan Facilities the proceeds of which are then advanced to DCC.

Promptly following the occurrence of a Standstill, each Standstill Creditor will notify the Standstill Cash Manager and the DCC Security Trustee of the amount of each of its individual tiered claims against DCC (adjusted subsequently, if appropriate) for the remainder of the Relevant Year during which the Standstill has occurred. Promptly following receipt of such notifications from each of the Standstill Creditors, the Standstill Cash Manager on behalf of the DCC Security Trustee shall notionally apply the balance then credited to the Debt Service Payment Account in accordance with the DCC Standstill Priority and (without double counting) credit each Standstill Ledger, Sub-Ledger and Sub-Sub Ledger with the amount, if any, credited to such Standstill Ledger, Sub-Ledger and Sub-Sub Ledger as a result of such notional application.

All monies credited on a monthly basis to the Debt Service Payment Account during the remainder of the Relevant Year shall be notionally applied by the Standstill Cash Manager on behalf of the DCC Security Trustee in accordance with the DCC Standstill Priority and each Standstill Ledger, Sub-Ledger and Sub-Sub Ledger shall be credited by the Standstill Cash Manager on behalf of the DCC Security Trustee (without double counting) with the amount, if any, credited to such Standstill Ledger, Sub-Ledger and Sub-Sub Ledger as a result of such notional application.

Each Standstill Creditor shall notify the Standstill Cash Manager and the DCC Security Trustee of the amount of each of its individual tiered claims against DCC for each Relevant Year during which the Standstill continues promptly upon the commencement of such Relevant Year and all monies credited each month to the Debt Service Payment Account during such Relevant Year shall continue to be notionally applied in accordance with the DCC Standstill Priority.

No amounts may be withdrawn from the Debt Service Payment Account during a Standstill to meet any Claim unless and until each Ledger, Sub-Ledger and Sub-Sub Ledger in respect of each prior ranking Claim has and remains credited with an amount equal to not less than 100% of the outstanding liability in respect of which such Ledger, Sub-Ledger and Sub-Sub Ledger has been established.

If on any day that a Claim of a Standstill Creditor (a "**Relevant Standstill Creditor**") represented by a Sub-Ledger or a Sub-Sub Ledger of the Relevant Standstill Creditor falls to be paid, there are insufficient sums credited to that Sub-Ledger or, as the case may be, Sub-Sub Ledger to meet the Relevant Standstill Creditor's Claim in full, then the Standstill Cash Manager on behalf of the DCC Security Trustee shall debit each other Sub-Ledger or, as the case may be, Sub-Sub Ledger which ranks equally with the Relevant Standstill Creditor's Claim *pro rata* according to the respective amounts credited to each other Sub-Ledger or, as the case may be, Sub-Sub Ledger (without double counting), by an amount equal to the lower of (a) the shortfall and (b) the aggregate amount then credited to each other equal ranking Sub-Ledger or, as the case may be, Sub-Sub Ledger and credit such amount to the relevant equal ranking Sub-Ledger or Sub-Sub Ledger of the Relevant Standstill Creditor which has fallen to be paid.

The Standstill Cash Manager on behalf of the DCC Security Trustee shall, in respect of (a) each Sub-Ledger or Sub-Sub Ledger of any Standstill Creditor (such Standstill Creditor, an "**Affected Standstill Creditor**") from which amounts have been debited to make good shortfalls to meet a Claim of the Relevant Standstill Creditor and (b) in respect of the Sub-Ledger or Sub-Sub Ledger of the Relevant Standstill Creditor which has been credited to make up the relevant shortfall, open and maintain a separate Ledger (each such Ledger, a "**Notional Liquidity Ledger**") and shall credit each Notional Liquidity Ledger in respect of each Affected Standstill Creditor (without double counting) with the amount debited from the corresponding Sub-Ledger or, as the case may be, Sub-Sub Ledger of that Affected Standstill Creditor and shall debit the Notional Liquidity Ledger of the Relevant Standstill Creditor with the amount so credited. A credit balance at any time on a Notional Liquidity Ledger of an Affected Standstill Creditor shall represent an advance (a "**Notional Liquidity Advance**") from that Affected Standstill Creditor to the Relevant Standstill Creditor. For so long as an Affected Standstill Creditor has a debit balance on its Notional Liquidity Ledger, all amounts notionally credited to the Sub-Ledger or Sub-Sub Ledger of the Relevant Standstill Creditor ranking equally with the Sub-Ledger or Sub-Sub Ledger of the Affected Standstill Creditor in accordance with the DCC Standstill Priority shall instead be applied, *pro rata* to the respective amounts credited to the relevant Notional Liquidity Ledgers of all equal ranking Affected Standstill Creditors, in reducing the credit balance on each relevant Notional Liquidity Ledger (with a corresponding credit to the Notional Liquidity Ledger of the Relevant Standstill Creditor) until such time as there is a zero balance on each relevant Notional Liquidity Ledger.

If after making any transfer from an equal ranking Sub-Ledger or Sub-Sub Ledger to the relevant Sub-Ledger or Sub-Sub Ledger of the Relevant Standstill Creditor there remains an insufficiency of funds available to DCC to meet that Claim, then DCC shall request the making of an L Advance in the amount of such shortfall.

The arrangements described above shall continue for so long as there is a Standstill. In the event that the Standstill is discharged, then the pre-Standstill cash allocation procedures described previously shall be reinstated. The DCC Security Trustee shall not be responsible for monitoring the performance of the Standstill Cash Manager.

If, following the implementation of a Standstill, there is an acceleration of Claims under the DCC STID then, upon such acceleration occurring, all monies credited to DCC's Accounts together with the proceeds of enforcement of any of the Security Documents shall be applied strictly in accordance with the priority of payments set out below (the "**DCC Post-Enforcement Payments Priorities**"):

(i) first, *pro rata* according to the respective amounts thereof, in or towards satisfaction of each Tier 1 Claim and in or towards satisfaction of each Tier 2 Creditor's Tier 2 Claim;

(ii) second, *pro rata* according to the respective amounts thereof:

(a) to the Overdraft Bank, in or towards satisfaction of any fees, interest and principal outstanding under the Overdraft Facility; and

(b) to the Account Bank, in or towards satisfaction of any accrued and unpaid fees and charges due to the Account Bank under the DCC Account Bank Agreement;

(iii) third, *pro rata* according to the respective amounts thereof:

(a) to the Issuer, in or towards satisfaction of the Issuer's Tier 3 Claim; and

(b) to each Authorised Lender in or towards satisfaction of such Authorised Lender's Tier 3 Claim;

(iv) fourth, *pro rata* according to the respective amounts thereof:

(a) to each DCC Hedging Counterparty, in or towards satisfaction of such Hedging Counterparty's Tier 4 Claim;

(b) to the Issuer, in or towards satisfaction of the Issuer's Tier 4 Claim; and

(c) to each DCC Finance Lessor, in or towards satisfaction of such DCC Finance Lessor's Tier 4 Claim;

(v) fifth, *pro rata* according to the respective amounts thereof:

(a) to the Issuer, in or towards satisfaction of the Issuer's Tier 5 Claim; and

(b) to each DCC Finance Lessor, in or towards satisfaction of such DCC Finance Lessor's Tier 5 Claim;

(vi) sixth, to the Issuer, in or towards satisfaction of the Issuer's Tier 6 Claim;

(vii) seventh, to the Issuer in or towards satisfaction of the Issuer's Tier 7 Claim;

(viii) eighth, to the Issuer, in or towards satisfaction of the Issuer's Tier 8 Claim;

(ix) ninth, to the Issuer, in or towards satisfaction of the Issuer's Tier 9 Claim;

(x) tenth, *pro rata* according to the respective amounts thereof:

(a) to each DCC Finance Lessor, in or towards satisfaction of such DCC Finance Lessor's Tier 10 Claim;

(b) to the Issuer, in or towards satisfaction of the Issuer's Tier 10 Claim;

(c) to each Authorised Lender, in or towards satisfaction of such Authorised Lender's Tier 10 Claim; and

(d) to each DCC Hedging Counterparty, in or towards satisfaction of such DCC Hedging Counterparty's Tier 10 Claim;

(xi) eleventh, to the Issuer, in or towards satisfaction of the Issuer's Tier 12 Claim;

(xii) twelfth, to the Issuer, in or towards satisfaction of the Issuer's Tier 13 Claim; and

(xiii) thirteenth, *pro rata* according to the respective amounts thereof:

(a) to WPD Finance, in or towards satisfaction of WPD Finance's Tier 11 Claim; and

(b) to the Issuer, in or towards satisfaction of the Issuer's Tier 14 Claim.

The proceeds of enforcement of the Guarantor Security will also be applied in accordance with the DCC Post-Enforcement Payments Priorities in circumstances where such enforcement occurs during a Standstill Period or following an acceleration of Claims under the DCC STID.

ISSUER CASH MANAGEMENT

The Issuer will establish or cause to be established on or before the Initial Issue Date sterling, euro and US dollar operating accounts (the "**Issuer Operating Accounts**") and an initial liquidity facility reserve account (the "**Initial Liquidity Account**"). The Issuer Accounts (as defined below) will be held with the Account Bank pursuant to an account agreement (the "**Issuer Account Bank Agreement**") dated on or about the Initial Issue Date between the Issuer, the Account Bank and the Issuer Security Trustee. DCC will act as Cash Manager of the Issuer and will, pursuant to the terms of the Master Framework Agreement manage amounts standing to the credit of the Issuer Accounts and any other accounts of the Issuer from time to time.

Each Liquidity Facility Agreement will require the establishment of a further liquidity facility reserve account ("**Further Liquidity Accounts**" which, together with the Initial Liquidity Account, are referred to as the "**Liquidity Accounts**" and, collectively with the Issuer Operating Accounts, are referred to as the "**Issuer Accounts**").

The Cash Manager will open and maintain in respect of the sterling denominated Issuer Operating Account a ledger in respect of each Series (a "**Series Ledger**") for the purpose of recording all payments made by or to the Issuer under the Intercompany Loan Agreement entered into in connection with such Series. The Cash Manager will therefore establish on or before the Initial Issue Date the Series 1 Ledger in respect of the Initial Intercompany Loan Agreement.

Prior to the service of an Enforcement Notice under the Issuer Deed of Charge all monies credited to a Series Ledger will rank for payment in accordance with the priority of payments ("**Issuer Pre-Enforcement Payments Priorities**") set out in the Issuer STID as set out below:

(i) first, *pro rata* according to the respective amounts thereof, in or towards satisfaction of the Relevant Series Proportion of the remuneration, costs and expenses of the Bond Trustee and Issuer Security Trustee;

(ii) second, in or towards satisfaction of, on a *pro rata* basis, (a) the Relevant Series Proportion of the remuneration, costs and expenses of the Paying Agents, the Agent Bank, the Registrar, the Transfer Agents, the Luxembourg Listing Agent and any other agents appointed under the Paying Agency Agreement or otherwise (collectively, the "**Agents**"), (b) the Relevant Series Proportion of the remuneration, costs and expenses of the Account Bank under the Issuer Account Bank Agreement, (c) the remuneration, costs and expenses of the Liquidity Facility Agent under the Liquidity Facility Agreement applicable to the relevant Series, (d) the remuneration, costs and expenses of the Class R Agent (if any) for the relevant Series, (e) the remuneration, costs and expenses of the Authorised Loan Facility Agent under each Authorised Loan Agreement (if any) for the relevant Series, (f) the Relevant Series Proportion of the costs and expenses of the Cash Manager and (g) the fees, expenses and premia of the Financial Guarantor for the relevant Series pursuant to the relevant I&I Agreement for the relevant Series;

(iii) third, *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 under the Liquidity Facility Agreement for the relevant Series, (b) all amounts of interest and principal due or overdue under the Class R Bonds to the extent that such Class R Bonds were re-sold to fund a New Money Advance and (c) all amounts of interest and principal due or overdue in respect of any drawing under an Authorised Loan Agreement to the extent that such drawing was made by the Issuer to fund a New Money Advance;

(iv) fourth, *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;

(v) fifth, *pro rata* according to the respective amounts thereof, in or towards satisfaction of (a) all amounts of interest due or overdue in respect of all of the Class A Bonds, Class B Bonds and Class R Bonds (if any) (in each case, other than any Subordinated Coupon Amounts in respect thereof), (b) all scheduled amounts payable to each Hedge Counterparty under any Currency Hedging Agreement entered into in respect of all of the Class A Bonds or the Class B Bonds (if any), (c) all amounts of underwriting commissions (other than Subordinated Commissions) due or overdue in respect of all of the Class R Bonds (if any), (d) all reimbursement sums owed under the relevant I&I Agreement to the Financial

Guarantor (if any) of the relevant Series in respect of payments of interest on any Class A Bonds of the relevant Series guaranteed by such Financial Guarantor and (e) all amounts of interest and commitment commissions due or overdue in respect of the Authorised Loan Facilities available to the Issuer (if any, other than any Subordinated Authorised Loan Amounts) established in connection with the relevant Series;

(vi) sixth, *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 Bonds, Class B Bonds and Class R Bonds (if any) of the relevant Series, (b) all principal exchange amounts due and payable to each Hedge Counterparty under any Currency Hedging Agreement entered into in respect of the Class A Bonds or the Class B Bonds of the relevant Series (if any), (c) any other sums due and payable to each Hedge Counterparty under any Hedging Agreement in respect of the Class A Bonds and Class B Bonds subject to (iv) and (v) above and (ix) below, (d) all reimbursement sums owed to the Financial Guarantor (if any) of the relevant Series under the relevant I&I Agreement in respect of payments of principal on the Class A Bonds of the relevant Series and (e) all amounts of principal due or overdue under the Authorised Loan Facility (if any) established for the relevant Series;

(vii) seventh, *pro rata* according to the respective amounts thereof, in or towards satisfaction of all amounts of (a) interest due or overdue on the Class C Bonds of the relevant Series (other than any Subordinated Coupon Amounts) and (b) all scheduled amounts due and payable to each Hedge Counterparty under any Currency Hedging Agreement entered into in respect of the Class C Bonds of the relevant Series;

(viii) eighth, *pro rata* according to the respective amounts thereof, in or towards satisfaction of (a) all amounts of principal due or overdue on the Class C Bonds of the relevant Series, (b) all principal exchange amounts due and payable to each Hedge Counterparty under any Currency Hedging Agreement entered into in respect of the Class C Bonds of the relevant Series, and (c) any other sums due and payable to each Hedge Counterparty under a Hedging Agreement in respect of the Class C Bonds subject to (iv) and (vii) above and (xiii) below;

(ix) ninth, in or towards satisfaction of any termination payment due or overdue to a Hedge Counterparty under any Hedging Agreement entered into in respect of the Class A Bonds or Class B Bonds which arises as a result of a default by such Hedge Counterparty;

(x) tenth, in or towards satisfaction of all amounts of interest due or overdue on the Class D Bonds of the relevant Series (other than any Subordinated Coupon Amounts);

(xi) eleventh, in or towards satisfaction of all amounts of principal due or overdue on the Class D Bonds of the relevant Series;

(xii) twelfth, *pro rata* according to the respective amounts thereof, in or towards satisfaction of (a) all Subordinated Liquidity Facility Amounts due or overdue under the Liquidity Facility Agreement provided in connection with the relevant Series, (b) all Subordinated Authorised Loan Amounts due or overdue under the Authorised Loan Facilities available to the Issuer provided in connection with the relevant Series and (c) any other indemnified amounts due or overdue to the Financial Guarantor of the relevant Series;

(xiii) thirteenth, in or towards satisfaction of any termination payment due or overdue to a Hedge Counterparty under any Hedging Agreement entered into in respect of the Class C Bonds which arises as a result of a default by such Hedge Counterparty;

(xiv) fourteenth, *pro rata* according to the respective amounts thereof, in or towards satisfaction of all Subordinated Coupon Amounts due or overdue in respect of the Class A Bonds, Class B Bonds and Class R Bonds (if any) of the relevant Series;

(xv) fifteenth, in or towards satisfaction of all Subordinated Coupon Amounts due or overdue in respect of the Class C Bonds of the relevant Series;

(xvi) sixteenth, in or towards satisfaction of all Subordinated Coupon Amounts due or overdue in respect of the Class D Bonds of the relevant Series; and

(xvii) seventeenth, the surplus, if any, to the Issuer or other persons entitled thereto.

After the service of an Enforcement Notice by the Issuer Security Trustee under the Issuer Deed of Charge, the Issuer Security Trustee (or any substitute cash manager appointed by the Issuer Security Trustee to act on its behalf) shall (to the extent that such funds are available) use funds standing to the credit of the Issuer Accounts to make payments in accordance with the following order of priority (the "**Issuer Post-Enforcement Payments Priorities**"):

(i) first, *pro rata* according to the respective amounts thereof, in or towards satisfaction of all of the remuneration, costs and expenses of the Bond Trustee and the Issuer Security Trustee and any receiver or receivers appointed by the Issuer Security Trustee pursuant to the Issuer Deed of Charge;

(ii) second, *pro rata* according to the respective amounts thereof, in or towards satisfaction of (a) all of the remuneration, costs and expenses of the Agents, (b) all of the remuneration, costs and expenses of the Account Bank under the Issuer Account Bank Agreement, (c) all of the remuneration, costs and expenses of each Liquidity Facility Agent under each Liquidity Facility Agreement, (d) all of the remuneration, costs and expenses of each Class R Agent, (e) all of the remuneration, costs and expenses of each Authorised Loan Facility Agent under each Authorised Loan Agreement available to the Issuer, and (e) all of the fees, expenses and premia of each Financial Guarantor pursuant to each I&I Agreement;

(iii) third, *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 under each Liquidity Facility Agreement, (b) all amounts of interest and principal due or overdue under the Class R Bonds to the extent that such Class R Bonds were sold to fund a New Money Advance and (c) all amounts of interest and principal due or overdue in respect of any drawing under any Authorised Loan Agreement to the extent that such drawing was made by the Issuer to fund a New Money Advance;

(iv) fourth, *pro rata* according to the respective amounts thereof, in or towards satisfaction of (a) all amounts of interest due or overdue in respect of all Class A Bonds, Class B Bonds and Class R Bonds (in each case, other than any Subordinated Coupon Amounts in respect thereof), (b) all sums due and payable to each Hedge Counterparty under any Hedging Agreement entered into in respect of the Bonds of any Class subject to (viii) below, (c) all amounts of underwriting commissions (other than Subordinated Commissions) due or overdue in respect of all Class R Bonds, (d) all reimbursement sums owed under the relevant I&I Agreement to each Financial Guarantor in respect of payments of interest on any Class A Bonds guaranteed by such Financial Guarantor and (e) all amounts of interest and commitment commissions due or overdue in respect of each Authorised Loan Facility (other than any Subordinated Authorised Loan Amounts);

(v) fifth, *pro rata* according to the respective amounts thereof, in or towards satisfaction of (a) all amounts of principal due or overdue in respect of all Class A Bonds, Class B Bonds and Class R Bonds, (b) all reimbursement sums owed to each Financial Guarantor under the relevant I&I Agreement in respect of payments of principal on Class A Bonds and (c) all amounts of principal due or overdue under each Authorised Loan Facility;

(vi) sixth, in or towards satisfaction of all amounts of interest due or overdue on the Class C Bonds of the relevant Series (other than any Subordinated Coupon Amounts in respect thereof);

(vii) seventh, in or towards satisfaction of all amounts of principal due or overdue on the Class C Bonds of the relevant Series;

(viii) eighth, in or towards satisfaction of any termination sum due or overdue to any Hedge Counterparty under any Hedging Agreement which arises as a result of a default by such Hedge Counterparty;

(ix) ninth, in or towards satisfaction of all amounts of interest due or overdue on all Class D Bonds (other than any Subordinated Coupon Amounts in respect thereof);

(x) tenth, in or towards satisfaction of all amounts of principal due or overdue on all Class D Bonds;

(xi) eleventh, *pro rata* according to the respective amounts thereof, in or towards satisfaction of (a) all Subordinated Liquidity Facility Amounts due or overdue under each Liquidity Facility Agreement, (b) all Subordinated Authorised Loan Amounts due or overdue under each Authorised Loan Facility available to the Issuer and (c) all other indemnified amounts due or overdue to each Financial Guarantor;

(xii) twelfth, *pro rata* according to the respective amounts thereof, in or towards satisfaction of all Subordinated Coupon Amounts due or overdue in respect of all Class A Bonds, Class B Bonds and Class R Bonds;

(xiii) thirteenth, in or towards satisfaction of all Subordinated Coupon Amounts due or overdue in respect of all Class C Bonds;

(xiv) fourteenth, in or towards satisfaction of all Subordinated Coupon Amounts due or overdue in respect of all Class D Bonds;

(xv) fifteenth, in or towards satisfaction of all amounts owing to the Cash Manager under the Master Framework Agreement; and

(xvi) sixteenth, the surplus, if any, to the Issuer or other persons entitled thereto.

Subject to the entrenched rights of the Issuer Security Trustee and the other Issuer Secured Creditors (including the Bond Trustee) the terms of the Issuer Pre-Enforcement Payments Priorities and the Issuer Post-Enforcement Payments Priorities may change if the Issuer issues further Series of Bonds or enters into further Authorised Loan Facilities in the future.

ADDITIONAL RESOURCES AVAILABLE

Finance Leases

Supply Agreements

By equipment supply agreements dated 26 March 1992 and 28 June 1996 (the "**Supply Agreements**"), DCC has supplied certain equipment to Abbey National March Leasing (1) Limited ("**Abbey National**") and Lloyds Plant Leasing Limited ("**Lloyds**"), respectively.

The equipment supplied under the Supply Agreements (the "**Equipment**") consists primarily of equipment for use in the water and sewerage operations of DCC, including generators, compressors, tanks, pipework, filter pressure vessels, pumps valves and other such process plant equipment. In addition, under the Supply Agreement entered into with Lloyds, certain services are also supplied. The Equipment is comprised of moveable equipment ("**Moveables**") and fixed equipment (that is, Equipment which is affixed to the real estate of DCC as a legal fixture, "**Fixtures**"). Moveables become Fixtures on attachment or fixture to DCC's real estate.

Pursuant to the terms of the Supply Agreements, DCC provides, *inter alia*, certain warranties customary for agreements of this nature and certain covenants relating to the supply of Equipment. The material rights and remedies of the Finance Lessors (as defined below) under the Supply Agreements shall be subject to the terms of the Common Terms Agreement and the DCC STID (see above for details).

Finance Leases

Each of Abbey National and Lloyds (each a "**Finance Lessor**" and together, the "**Finance Lessors**") has leased the items of Equipment purchased by them under the Supply Agreements to DCC on the terms, and subject to the conditions, set out in the lease agreements dated 26 March 1992 and 28 June 1996 between DCC as lessee and the respective Finance Lessor as lessor (each a "**Finance Lease**" and, together, the "**Finance Leases**").

The principal lease periods under the Finance Leases with Lloyds and Abbey National are 25 years and 20 years from the date of commencement of such lease periods (each a "**Principal Lease Period**"). The leasing of the Equipment under the Finance Leases, subject to any full or partial early termination (see below), is for a period (a) in respect of Fixtures (other than under the Finance Lease with Lloyds where certain extensions are possible), of no longer than the respective Principal Lease Period and (b) in respect of Moveables, a period of no longer than the respective Principal Lease Period, save that the leasing of certain Moveables may be extended for further 12 month periods, or until the end of the useful life of any such Moveable, at the option of DCC.

Terms and Conditions

Each Finance Lease is to be amended as of the Initial Issue Date so as to be subject to the Common Terms Agreement, which will set out certain of the representations and warranties, covenants and events of default which will apply to the Finance Leases as of such date (see "*Common Terms Agreement*" above). In addition, certain of the material terms of each of the Finance Leases are summarised below:

Rental

DCC is obliged to pay rental payments ("**Rental**") on an annual basis in advance of 1 April of each year (each, a "**Rental Payment Date**"). The Rental, as stated in each Finance Lease, assumes a specific rate of interest and, should the actual rate of interest be other than the assumed rate, each Finance Lease provides for adjusting payments to the Rental to be made/received by DCC to/from the relevant Finance Lessor by way of additional, or rebates of, Rental.

The annual Rental is calculated in accordance with certain assumptions and based upon an annual cash flow report, both of which, together with the Rental, are subject to adjustment from time to time. Rentals may be adjusted for the following annual periods on the occurrence of certain events, including *inter alia*, (i) by the relevant Finance Lessor where applicable variable assumptions change, where a replacement cash flow report is produced, where part of the Equipment is the subject of an early termination, or where the tax assumptions (such as the rate of corporation tax, or the rate of writing down allowances available to the Finance Lessor) prove incorrect, or (ii) by DCC under the Abbey National Finance Lease, where DCC has exercised certain funding options to adjust its obligations in respect of the interest rate element of the Rental payable pursuant to the terms of the relevant Finance Lease. In particular, DCC may pay fixed rate tranches of the Rental, at its election, in accordance with the terms of the Finance Leases.

VAT is chargeable on the Rental due under the Finance Leases.

General Payment Provisions

Default interest at a rate of 1.5 per cent. under the Lloyds Finance Lease and 2 per cent. under the Abbey National Finance Lease above applicable reference rates is payable on any late payments.

All payments of principal and interest under each Finance Lease will 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, DCC will be obliged to pay such additional amounts as will result in the receipt by the relevant Finance Lessor of such amounts as would have been received by it if no such withholding or deduction had been required.

DCC Obligations

In addition to the representations and warranties made by DCC and the obligations placed upon DCC pursuant to the Common Terms Agreement, the Finance Leases also include certain standard finance lease representations, warranties and covenants.

In particular, DCC is required, in accordance with the Finance Leases, *inter alia*, (1) to maintain, service, repair and overhaul the Equipment so as to keep the Equipment in good repair, condition and working order in accordance with customary practice of a prudent and responsible water and sewerage undertaking; (2) promptly to replace any item of Equipment which is worn out, obsolete or damaged; (3) to maintain third party liability and property and damage insurances in respect of the Equipment, satisfactory to the Finance Lessors; and (4) to perform all acts or provide all assistance necessary and/or desirable to preserve each Finance Lessor's tax benefits and/or position under the Finance Lease, including entering into elections that entitle the relevant Finance Lessor to claim capital allowances on any of the Equipment which constitutes Fixtures.

A material breach of any of these representations and/or obligations (to the extent not waived) will oblige DCC to prepay all sums due and payable under the relevant Finance Lease. Such prepayment shall be funded solely from Permitted Indebtedness (as summarised above, see "*Common Terms Agreement*") and subject to the Common Terms Agreement and the DCC STID. If DCC does not make such prepayment in accordance with the Common Terms Agreement, an Event of Default under the Common Terms Agreement will arise (to the extent not waived) and the Standstill Period will automatically commence (see "*DCC STID – Standstill*" above).

Indemnities

Each Finance Lease contains a general indemnity whereby DCC agrees to indemnify the relevant Finance Lessor (and/or, in respect of certain indemnities under certain of the Finance Leases, the relevant Finance Lessor corporate group) on demand against all losses, payments, damages, liabilities, claims, proceedings, actions, penalties, fines or other sanctions of a monetary nature, costs and expenses (including legal expenses, out-of-pocket expenses and, in certain cases, costs of management time) in any way associated with the transactions contemplated in the relevant Finance Lease ("**Losses**") other than Losses (i) arising as a result of the wilful default or negligence of the relevant Finance Lessor or (ii) compensated for elsewhere in the relevant Finance Lease.

Typically, although not always in each case, under the Finance Leases, DCC shall indemnify (and keep indemnified) the relevant Finance Lessor against all Losses incurred or suffered by it (and/or its corporate group) and, *inter alia*:

- relating to or arising indirectly or directly from the condition, testing, delivery, design, manufacture, purchase, importation or exportation of, registration, ownership, possession, control, surveying, engineering, contracting, installation, affixation of or to land or buildings, use, operation, maintenance, repair, service, modification, replacement or otherwise in connection with the relevant Equipment, or any sale or other disposition of the relevant Equipment following termination of the relevant Finance Lease;
- which may at any time be incurred on the grounds that any design, articles or material in the relevant Equipment or the operation or use thereof constitutes an infringement of any intellectual property right or any other right whatsoever;
- which are incurred by the relevant Finance Lessor by reason of any failure of DCC to comply with its obligations under the relevant Finance Lease (or other related documentation); and
- relating to, connected with or incidental to the protection, preservation or enforcement or attempted enforcement of any right or remedy conferred on the relevant Finance Lessor under the relevant Finance Lease (or other related documentation).

Tax Indemnities

Under the terms of the Finance Leases, DCC is required to compensate the Finance Lessors for certain tax events by variation of the Rental payment amounts and/or by contractual indemnity payments. Typically, although not always in each case, Finance Lease tax indemnities include, *inter alia*:

- to the extent that any sum received by a Finance Lessor or directly by a third party, in either case by way of indemnity, is treated as taxable in the hands of the relevant Finance Lessor where the corresponding obligation of the Finance Lessor to which such indemnity relates is not deductible for tax purposes, that DCC shall indemnify such Finance Lessor for such sum/taxation (after taking into account any credit, relief or allowance the Finance Lessor may obtain in respect of that sum) as may be required to keep the Finance Lessor whole;
- to the extent that any sum payable by or on behalf of a Finance Lessor to DCC under the relevant Finance Lease where such sum is payable out of sums brought into account for tax purposes, is not permitted as a deduction in computing the profits of such Finance Lessor for tax purposes in the accounting period of the Finance Lessor in which it is payable, that DCC shall pay to such Finance Lessor by way of indemnity such sum certified by such Finance Lessor to DCC as shall (after taking into account any taxation suffered by such Finance Lessor) place such Finance Lessor in the same position as it would have been in had the relevant payment been deductible;
- that DCC shall pay on demand all stamp, documentary, registration, excise, property or other like duties, including any such duties or taxes payable by a Finance Lessor and any penalties or interest thereon, or taxes imposed on or in connection with any of the Finance Leases (and/or related documents) which arise or become payable and shall indemnify such Finance Lessor against any liability arising by reason of any delay or omission by DCC to pay any such duties or taxes; and
- that DCC shall pay any VAT suffered by the Finance Lessors in respect of any amounts due under the terms of the Finance Leases and any irrecoverable VAT suffered by the Finance Lessor.

There are provisions in the Finance Leases to avoid double counting under the indemnity and Rental adjustment clauses.

All indemnities survive any termination of the leasing of the Equipment under the Finance Leases and the termination of the Finance Leases themselves.

Termination of Finance Leases

Subject to the terms of the DCC STID (including the provisions applying during a Standstill Period), the leasing of part or all of the Equipment under the Finance Leases may be terminated on the occurrence of any of the DCC Events of Default specified in the Common Terms Agreement.

In addition, subject to the terms of the Common Terms Agreement, the DCC STID and the Finance Leases (as amended and supplemented) and provided DCC is able to fund such termination or prepayment from Permitted Indebtedness (as specified above, see "*Common Terms Agreement*"):

- DCC may, for any reason, terminate the leasing of all or part of the Equipment under any Finance Lease and DCC may prepay all Rentals due thereunder in advance of the expiry of the relevant lease period; and
- each Finance Lessor may terminate the leasing of the Equipment under its Finance Lease if (a) an illegality event in respect of that Finance Lessor occurs; (b) a total loss of its leased Equipment occurs; or (c) in respect of Lloyds, it exercises its option to terminate the relevant Finance Lease on 1 April 2018.

If DCC fails to make any such prepayment in accordance with the Common Terms Agreement, a DCC Event of Default will arise under the Common Terms Agreement and the Standstill Period will automatically commence (see "*DCC STID – Standstill*" above).

Termination payments vary according to the termination event which takes place and the date thereof. They are calculated, broadly speaking, by the production of a revised cashflow as at the date of the relevant termination and based upon certain assumptions.

Repossession of Moveables on Termination

Pursuant to the terms of the Supply Agreements, the Finance Lessors purchased the legal and beneficial title to Moveables. Upon the affixing of certain Moveables to the real estate of DCC in accordance with the relevant Finance Leases, such Moveables became Fixtures. Upon the creation of such Fixtures, legal and beneficial title to the same was transferred from the relevant Finance Lessor to DCC (albeit that, for fiscal purposes only, title is deemed to rest with the relevant Finance Lessors).

Following a termination event under the Finance Leases, DCC is required, at its own cost and expense, to redeliver possession of any Equipment which remains a Moveable to the relevant Finance Lessor. The Finance Lessors shall sell, if possible, the returned Moveables and shall share the net sale proceeds of any such sale with the other DCC Secured Creditors.

Insurance and Total Loss

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

DCC bears the full risk of any total loss (which definition shall include requisitions, compulsory acquisitions, or other such actions which continue beyond a prescribed time period) or any damage to all or a material part of the Equipment.

Related Guarantee

The guarantee from Hyder (previously Welsh Water plc) in favour of Abbey National in connection with the relevant Finance Lease will be released and discharged on or before the Initial Issuer Date.

The Gen Re Swap

On 15 March 1994, DCC entered into an interest rate swap transaction with Gen Re Securities Limited (the "**Existing DCC Hedge Counterparty**") in order to hedge a proportion of its floating rate interest exposure under the Abbey National Finance Lease (the "**Gen Re Swap**").

The Gen Re Swap is evidenced by a confirmation dated 28 March 1995 which is in turn governed by the terms of 1987 ISDA Interest Rate and Currency Exchange Agreement containing standard ISDA events of default and termination events including a termination event in the event that a party to the Gen Re Swap is required to gross-up for tax due to, *inter alia*, a change in tax law.

The Gen Re Swap contains optional rights of early termination permitting either party to terminate the Gen Re Swap on 1 April 2004 and permitting DCC to terminate the Gen Re Swap in whole or in part on five business days' notice.

The Existing DCC Hedge Counterparty will on or before the Initial Issue Date become a party to the DCC STID and the Common Terms Agreement which will act as an amendment to the events of default otherwise applicable to the Gen Re Swap for the purposes of taking the benefit of the representations, warranties and covenants of DCC and the Guarantors and pursuant to which, except as provided below, the events of default and termination events in relation to acts of, or circumstances relating to, DCC will be overridden by the DCC Events of Default under the Common Terms Agreement.

Accordingly, the Gen Re Swap may, save to the extent described below, be terminated by the Existing DCC Hedge Counterparty only upon the occurrence of a DCC Event of Default. The Existing DCC Hedge Counterparty will, notwithstanding the provisions of the Common Terms Agreement, additionally have the right to terminate the Gen Re Swap if:

- the Abbey National Finance Lease is terminated; or
- if it is required, due to a change in tax law, to gross-up any payment due from it under the Gen Re Swap or if there is a substantial likelihood that it will be required so to gross-up due to action taken by a tax authority or brought in court.

Furthermore, DCC and Gen Re will retain the option to terminate the Gen Re Swap on 1 April 2004 and DCC will retain its option to terminate the Gen Re Swap in whole or in part on five business days' notice.

If DCC fails to pay any termination sum due as a result of the occurrence or implementation of any such termination event, a DCC Event of Default will arise under the Common Terms Agreement and a Standstill Period will automatically commence (see "*DCC STID – Standstill*" above).

Local Authority Loans

DCC has outstanding loans of approximately £5,855,000 from certain local authorities in Wales. The local authorities who have made these loans available to DCC have not acceded, and will not be required to accede, to the Common Terms Agreement, the DCC STID or the Intercreditor Arrangements.

Class R Bonds

The proceeds of the issue of the Class R Bonds will immediately be applied by the Issuer in the repurchase of the Class R Bonds, which the Issuer is permitted to do under its Memorandum of Association and pursuant to the Conditions applicable thereto. The Class R Bonds so repurchased will not be cancelled but will remain within the clearing systems and will be available to be resold from time to time subject to certain criteria set out in Chapter 14 under "*Subscription and Sale*" and specified in the Class R Underwriting Agreement. Any Class R Bonds so resold may be repurchased by the Issuer on any day and will be repurchased by the Issuer no later than the Issuer Payment Date which immediately follows their resale, provided that no Issuer Event of Default under the Bonds has occurred and is continuing. Any Class R Bonds will be repurchased by the Issuer at par plus, in the case of any repurchase, the interest accrued to the date of such repurchase. The Issuer will not be required to repurchase any Class R Bonds on an Issuer Payment Date to the extent that any Class R Underwriter fails to finance such repurchase by subscribing for new Class R Bonds. In such event, the Class R Bonds which are not repurchased will remain in issue and interest will continue to accrue on them. Whilst held by, for or on behalf of the Issuer, or any other member of the Financing Group, or any of their respective affiliates, the Class R Bonds will not accrue interest and will not confer any voting rights.

The proceeds of the Class R Bonds which are resold by the Issuer will be applied in making R Advances under the Initial Intercompany Loan Agreement from time to time. (See "*Intercompany Loan Agreements*" above.)

The Issuer will covenant that it will use its best endeavours on and from 31 March 2006 to repurchase all Class R Bonds then outstanding. After 31 March 2006 any outstanding Class R Bonds will bear interest at a higher margin and they will cease to revolve.

Pursuant to the Class R Underwriting Agreement, the Class R Agent will be appointed as the agent of the Class R Underwriters to carry out certain administrative functions in relation to the repurchase and resale of the Class R Bonds and will charge a fee for the provision of such services as and when it arises.

Authorised Loan Facilities

The Issuer and DCC will each enter into a facility agreement (each an "**Initial Authorised Loan Facility**") with an aggregate facility amount of £150,000,000 with the Initial Authorised Lender on or about the Initial Issue Date. The Initial Authorised Loan Facility made available to DCC is a revolving credit facility which is available to DCC for working capital and capital expenditure requirements from the Initial Issue Date until the final maturity date of the day before the fifth anniversary of the Initial Issue Date. The Initial Authorised Loan Facility made available to the Issuer is a revolving credit facility which is available to the Issuer to fund working capital and capital expenditure requirements of DCC from the Initial Issue Date until the final maturity date of the day before the fifth anniversary of the Initial Issue Date.

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

Each of DCC and the Issuer makes representations and warranties to the Initial Authorised Lender on terms as set out, respectively, in the Common Terms Agreement and the Master Framework Agreement. Certain representations and warranties will be repeated at the date of drawing a loan and on certain Issuer Payment Dates or DCC Payment Dates, as the case may be.

Each of DCC and the Issuer makes covenants and undertakings to the Initial Authorised Lender on terms as set out, respectively, in the Common Terms Agreement and the Master Framework Agreement.

The DCC Events of Default under the Common Terms Agreement will apply to DCC under its Initial Authorised Loan Facility (see "*Common Terms Agreement*" above). Events of default similar to the Issuer Events of Default under the Bonds will apply to the Issuer under its Initial Authorised Loan Facility (see Condition 11 in Chapter 6 under "*Terms and Conditions of the Bonds*").

The ability of the Initial Authorised Lender to accelerate any sums owing to it under DCC's Initial Authorised Loan Facility upon or following the occurrence of a DCC Event of Default thereunder is subject to the DCC STID. The ability of the Initial Authorised Lender to accelerate any sums owing to it under the Issuer's Initial Authorised Loan Facility upon or following the occurrence of an event of default thereunder is subject to the Issuer STID.

The Issuer and/or DCC may enter into further Authorised Loan Facilities on terms similar to those in the relevant Initial Authorised Loan Facility except that any Authorised Loan Facilities entered into by DCC for working capital and capital expenditure purposes will be subject to an aggregate cap of £50,000,000 (indexed), and the aggregate amount of drawings under the Overdraft Facility and such Authorised Loan Facilities from time to time shall not, in the aggregate, exceed £50,000,000 (indexed). Each additional Authorised Lender will be given the benefit of the Issuer Security or the DCC Security, as the case may be, and will be required to accede to the Issuer STID or the DCC STID, as the case may be.

The Liquidity Facilities

Liquidity facilities (each a "**Liquidity Facility**") will be established under agreements (each a "**Liquidity Facility Agreement**") entered into in connection with each Series of Bonds issued.

Each Liquidity Facility Provider must be a bank which as at the relevant Issue Date has a rating assigned for its short-term unsecured, unsubordinated and unguaranteed debt obligations of at least A-1/P-1/F-1 from the relevant Rating Agencies or such other short-term rating as is commensurate with the original issue ratings assigned to the Class A Bonds, Class B Bonds and Class R Bonds remaining outstanding from each of the Rating Agencies (the "**Requisite Ratings**").

Under the terms of each Liquidity Facility Agreement, one or more Liquidity Facility Providers will provide a 364-day commitment in an aggregate amount specified in each Liquidity Facility Agreement to permit drawings to be made in circumstances where (i) the Issuer has or will have insufficient funds

available on an Issuer Payment Date to pay in full its obligations in respect of scheduled interest on the Class A Bonds, Class B Bonds, Class R Bonds and (subject to certain limits) Class C Bonds and scheduled interest on its Authorised Loan Facilities, or (ii) DCC has or will have insufficient funds available on a DCC Payment Date to pay in full its obligations in respect of scheduled interest on its Authorised Loan Facilities or the notional scheduled interest payments under the DCC Finance Leases (each a "**Liquidity Shortfall**"). The amount which may be drawn under a Liquidity Facility Agreement applicable to any Series to make up any Liquidity Shortfall arising on the Class C Bonds of the relevant Series shall be limited to the proportion that the Outstanding Principal Amount of the Class C Bonds of that Series bears to the aggregate Principal Amount Outstanding of the Class A Bonds, Class Bonds, Class R Bonds (if any) and Class C Bonds of that Series. No drawings will be permitted under any Liquidity Facility Agreement in respect of any Liquidity Shortfall on the Class D Bonds.

The Cash Manager on behalf of the Issuer may also, at any time, replace any Liquidity Facility Provider provided that such Liquidity Facility Provider is replaced by a bank with Requisite Ratings and all amounts outstanding to such Liquidity Facility Provider are repaid in full.

Amounts drawn by the Issuer under a Liquidity Facility (except by way of a Standby Drawing) will be lent by the Issuer to DCC as an L Advance under the relevant Intercompany Loan Agreement (see "*Intercompany Loan Agreements*" above). The Issuer will repay each drawing under a Liquidity Facility Agreement upon repayment of the corresponding amount of the relevant L Advance under the relevant Intercompany Loan Agreement. Amounts repaid may, subject to various conditions precedent, be redrawn. The Initial Liquidity Facility Providers will be The Royal Bank of Scotland plc and Lloyds TSB Bank plc.

Each Liquidity Facility Agreement will provide that if (i) at any time the rating of the short-term, unsecured, unsubordinated and unguaranteed debt obligations of the relevant Liquidity Facility Provider falls below the Requisite Ratings or (ii) the relevant Liquidity Facility Provider does not renew such Liquidity Facility prior to the expiry of the 364-day period, the Issuer will either:

- request (in the case of (i) above) such Liquidity Facility Provider, or (in case of (ii) above) all parties then comprising the Liquidity Facility Provider in relation to that Liquidity Facility, to pay into the relevant Liquidity Account or other such agreed account established for the Series to which such Liquidity Facility relates, an amount equal to (in the case of (i) above), the affected party's undrawn commitment under such Liquidity Facility or (in the case of (ii) above), all commitments then available under such Liquidity Facility (a "**Standby Drawing**"); or

- (in the case of (i) above) replace each affected party with a party having the Requisite Ratings (whether by way of novation of the relevant Liquidity Facility Agreement or the entry into of a new Liquidity Facility Agreement with a party having the Requisite Ratings).

The Standby Drawing will generally be repayable only if the relevant Liquidity Facility Provider is re-rated with the Requisite Ratings or a replacement liquidity facility on terms acceptable to the Rating Agencies is entered into or if and to the extent such facility is no longer required to maintain the original issue ratings on the Class A Bonds, the Class B Bonds or the Class R Bonds from the relevant Rating Agencies. The proceeds of the Standby Drawing will be placed in the relevant Liquidity Account over which the Issuer will grant security pursuant to the terms of the Issuer Deed of Charge.

Interest will accrue on any drawing (including a Standby Drawing) made under the Liquidity Facility provided by the Initial Liquidity Facility Providers at a reference rate per annum plus a margin except where a Standby Drawing has been outstanding for 60 months, in which case the margin will increase by an agreed amount (the "**LF Step-Up**") until such drawing is repaid. Under the Initial Liquidity Facility Agreement, the Issuer will also be 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 (together with the LF Step-Up "**Subordinated Liquidity Facility Amounts**"). 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 Issuer Security pursuant to the Issuer Deed of Charge, all indebtedness outstanding under any Liquidity Facility (other than Subordinated Liquidity Facility Amounts) will rank in priority to the Bonds.

Hedging Agreements

Hedging Strategy

DCC and the Issuer will enter into hedging transactions in accordance with an agreed hedging strategy, pursuant to the Common Terms Agreement and Master Framework Agreement, respectively. This, *inter alia*, will require that DCC and the Issuer do not maintain any open currency positions and that they enter into appropriate hedging instruments to limit their exposure to interest rate fluctuations to a prudent level. DCC and the Issuer will be prohibited from entering into any form of hedging arrangement or swaps contract of a speculative nature or otherwise than in accordance with the agreed hedging strategy. DCC and the Issuer will maintain the hedging strategy over time in accordance with good industry practice and regulatory developments.

Initial Hedging Agreements

Prior to the Initial Issue Date, DCC entered into certain interest rate and currency swap transactions in order to take advantage of the then market conditions and establish a hedge in relation to the interest rate and currency exposure that the Issuer will have in relation to the Floating Rate Bonds and Bonds denominated in euro or US dollars issued on the Initial Issue Date. The rights and obligations of DCC under such transactions will either be cancelled or novated to the Issuer in consideration of the Issuer agreeing to enter into the Initial Intercompany Loan Agreement with DCC on or about the Initial Issue Date. The Issuer will enter into the novated transactions and certain further swap transactions with the Initial Hedge Counterparties. The Issuer will thus hedge its interest rate and currency exposure in respect of Sub-Classes of Bonds that accrue interest at a floating rate (other than Class R Bonds) or are denominated in euro or US dollars. Payments will be made between the Issuer and the Initial Hedge Counterparties under the Initial Hedging Agreements on Issuer Payment Dates.

Under the terms of the Initial Hedging Agreements, in the event that the ratings of the Initial Hedge Counterparties fall below the required credit ratings and, as a result the ratings of the relevant Classes of Bonds may be downgraded below the original issue rating, the relevant Initial Hedge Counterparty will either: (i) provide collateral for its obligations; (ii) arrange for its obligations under the relevant Initial Hedging Agreement to be transferred to, or guaranteed by, an appropriate Hedge Counterparty with the required credit ratings, or, with the prior consent of the Rating Agencies, an entity that has a lesser rating (to the extent that such action does not cause a reduction in the original issue ratings of the relevant Classes of Bonds); (iii) arrange for the appointment of a co-obligor with such ratings as, when combined with the relevant Initial Hedge Counterparty's then current ratings, will not cause a reduction in the original issue ratings of the relevant Classes of Bonds; or (iv) take such other action agreed with the relevant Rating Agencies that will not lead to a reduction in the original issue ratings of the relevant Classes of Bonds.

The Initial Hedge Counterparties will be obliged to make payments under the Initial Hedging Agreements without any withholding or deduction of taxes, unless required by law. If any such withholding or deduction is required by law, the Initial Hedge Counterparties will be required to pay any such additional amount as is necessary to ensure that the net amount received by the Issuer will equal the full amount the Issuer would have received had no such deduction or withholding been required. The Issuer will make payments under the Initial Hedging Agreements subject to any withholding or deduction of taxes required by law, but will not be required to pay any additional amount to any Initial Hedge Counterparty in respect thereof. However, in either case, if any such withholding or deduction is required, which cannot be avoided by both parties using reasonable endeavours to avoid such withholding or deduction, the Initial Hedge Counterparty may terminate the relevant Initial Hedging Agreement.

The Issuer will have rights to terminate an Initial Hedging Agreement, in certain circumstances, relating to the relevant Initial Hedge Counterparty (or, in certain circumstances, any credit support provider relating to it) including: a failure to pay amounts when due; the occurrence of an insolvency event; a breach of a term of the Initial Hedging Agreement or any credit support document; a merger without assumption; a default under specified types of transaction; and in the case of an event of illegality under the swap transactions.

Each Initial Hedge Counterparty's rights to terminate its Initial Hedging Agreement will be restricted to: (i) a failure by the Issuer to make a payment under the Initial Hedging Agreement when due; (ii) certain insolvency-related events with respect to the Issuer; (iii) illegality affecting the Initial Hedging Counterparty's ability to make or receive a payment; and (iv) where either the Hedge Counterparty or the Issuer is required to withhold for tax, which cannot be avoided, as described above. Each Initial Hedge Counterparty will be party to the Issuer STID and its rights (including, in particular, its rights to receive any termination payment) will be governed thereby and subject thereto.

Accordingly, any termination payment will be paid to an Initial Hedge Counterparty in accordance with the Issuer Pre-Enforcement Payments Priorities or the Issuer Post-Enforcement Payments Priorities, as the case may be.

In addition to the above, the Issuer and each Initial Hedge Counterparty will have the right to terminate a relevant Initial Hedging Agreement upon a delivery of a notice by the Bond Trustee, under Condition 11 of the Bonds, that the Bonds have become immediately due and payable. Further, the Issuer and each Initial Hedge Counterparty have termination rights if the Issuer redeems any of the relevant Classes of Bonds prior to their Expected Maturity Date.

OTHER TRANSACTION DOCUMENTS

Account Bank Agreements

Pursuant to the DCC Account Bank Agreement and the Issuer Account Bank Agreement, the Account Bank will agree to hold the Issuer Accounts and the DCC Accounts. The Cash Manager will manage the Issuer Accounts on behalf of the Issuer pursuant to the Master Framework Agreement, (see "*Issuer Cash Management*" above).

Corporate Services Agreement

Pursuant to a corporate services agreement (the "**Issuer Corporate Services Agreement**"), Maples and Calder will also provide certain corporate services to the Issuer.

Tax Deed of Covenant

Under the terms of the Tax Deed of Covenant to be entered into on or before the Initial Issue Date, each of the Issuer, DCC, Holdings, Glas Securities, Glas, Hyder and HUH will give certain representations, warranties and covenants, *inter alia*, (i) as to tax status and (ii) to the effect that they have not taken and will not take any steps which have had or will have the effect of rendering the Issuer liable to tax which is primarily the liability of another company. The obligations of HUH and Hyder under the Tax Deed of Covenant will be guaranteed by WPDH.

CHAPTER 5

INVESTMENT CONSIDERATIONS

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 certain events below could lead to, amongst other things:

(i) a DCC Event of Default under an Intercompany Loan Agreement;

(ii) an Issuer Event of Default under the Bonds or acceleration of the Bonds;

(iii) non-payment in respect of the Class B Bonds, Class R Bonds, Class C Bonds or Class D Bonds;

(iv) non-payment in respect of the Class A Bonds if, additionally, MBIA were to default on its obligations under any Bond Policy; and

(v) non-payment in respect of unguaranteed amounts under the Class A Bonds.

It 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.

Regulatory and Competition Considerations

The water industry is subject to extensive legal and regulatory controls, and DCC 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 and Ofwat could have a material adverse effect on the operations and financial condition of DCC.

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 DCC 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 (as defined below), no assurance can be given that the laws, regulations, regulatory standards or policies will not change in a manner that could adversely affect the operations of DCC.

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

Licence

Under the WIA, the conditions of DCC's Licence may be modified by the DGWS with the consent of DCC. If the DGWS and DCC cannot agree to the modifications, the conditions may be modified by the DGWS without the consent of DCC following a reference on the proposed modifications to the Competition Commission. In addition, the Assembly has a power to veto certain proposed modifications agreed by the DGWS and DCC and other proposed modifications which have been agreed by the DGWS and DCC may be referred by it for consideration by the Competition Commission. The area of appointment of DCC can also be varied in accordance with a so-called ''inset'' appointment (see Chapter 8 under ''*Termination of a licence*''). Modifications to the Licence may also be made without DCC'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.

Ofwat has proposed certain modifications to DCC's Licence to which DCC has consented. These modifications cover procurement of services and control of operations, strengthening the financial ring-fence, corporate governance and availability of market and other information (see Chapter 11: ''*Glas Cymru Cyfyngedig*''). The DGWS served notice on 7 March 2001 that these modifications would be made. There was a 28 day period for representations and objections to be raised in respect of such modifications which closed on 4 April 2001. The Assembly confirmed in a letter to Glas on 16 March 2001 that it would not oppose the proposed modifications. Ofwat has not yet announced that the proposed modifications have been implemented. (See Chapter 8: ''*Water Regulation – Licences*''.)

Termination of the Licence

Under the terms of the Licence, the minimum duration of DCC's appointment is 25 years from 1 September 1989. The first date on which the Secretary of State (as defined below) may terminate the appointment, without DCC's consent, is 2014 provided notice of at least 10 years has been given (i.e., in 2004). Upon expiry, there can be no certainty that DCC would be re-appointed. Ofwat anticipates that the Secretary of State will, in due course, seek Ofwat's advice on an assessment of each Regulated Company's performance in relation to termination of licences. During the 12 months from the date hereof, Ofwat intends to clarify these expectations with the DETR (as defined below).

DCC's Licence may also be transferred from DCC at any time following the making of a special administration order.

Draft Water Bill

On 6 November 2000, a draft Water Bill, which contains certain proposed changes to the regulatory system applicable to the water industry, was published for consultation. One of the most significant proposed changes in the draft Water Bill is a new power for the DGWS, the Secretary of State and the Assembly 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. There is also an amendment to the duties of the DGWS, the Secretary of State and the Assembly who would be 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 (see Chapter 8: "*Water Regulation – The Draft Water Bill*").

In the light of responses to the consultation paper and recent industry developments, the UK Government has concluded that further work on options for extending competition in the water industry needs to be undertaken, and, on 17 April 2001, it announced that it would publish a further consultation paper in the summer of 2001. So far, the UK Government has not announced a proposed timetable for introducing the draft Water Bill to Parliament, and it is not possible, therefore, to assess the likelihood or effect of the implementation of the draft Water Bill in its current (or any other) form.

Competition in the Water Industry

The UK Competition Act 1998 contains prohibitions relating to anti-competitive agreements and conduct and powers of investigation and enforcement (see Chapter 8 under "*Water Regulation – 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 10 per cent. of turnover for up to three years for infringement.

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 UK Government has indicated that it hopes 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 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 Chapter 8 under "*Competition in the Water Industry*". It is not possible to assess if, or how, such methods will affect the interests of Bondholders.

DCC Revenue Considerations

The revenues generated by DCC from its water and sewerage business may not be sufficient to enable it to make full and timely payment of amounts due under, *inter alia*, the Intercompany Loan Agreements. In addition to the regulatory and competition risks described above which could adversely affect the revenues of DCC, other potential events which could result in DCC having insufficient revenues to meet its financing obligations include:

Price Review

Periodic reviews of price limits are carried out at five-yearly intervals by the DGWS. There is no assurance that price limits will generate sufficient revenues to enable DCC 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, there are no requirements on the DGWS 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 and in determining whether or not to make allowance for the "embedded" costs of fixed rate debt.

Whilst giving no guarantees as to his future approach, the DGWS has said that he regards the current periodic review methodology as "robust" (see the statement by the DGWS in Appendix B: "*Ofwat Letter*"). He has also indicated that companies such as DCC will be treated no differently from other Regulated Companies, particularly as regards the allowable return on capital. Further, if a Regulated Company disputes the DGWS's price limits or infrastructure charge limits, it can require the DGWS to refer the determination to the Competition Commission.

As described in Chapter 8 under "*Interim Determinations of K*", Interim Determinations of price limits may be made between five yearly reviews in specified circumstances, including, in the case of DCC, those circumstances caught by the "shipwreck clause" (see below). In contrast to periodic reviews, the methodology to be applied for Interim Determinations is set out in detail in DCC's Licence and the scope for discretion is narrower. There can, however, be no assurance that if an adjustment is made it will provide adequate revenue compensation to DCC.

The DGWS has agreed (subject to the 28-day statutory consultation period) to DCC's request that the "shipwreck clause" be re-inserted in the Licence. This will permit DCC, or the DGWS, to request an Interim Determination if the regulated business either suffers a substantial adverse effect, which could not have been avoided by prudent management action, or if it enjoys a substantial favourable effect, which is fortuitous and not attributable to prudent management action. (See Chapter 8: "*Water Regulation – Substantial Adverse or Favourable Effect Shipwreck Clause*").

Deviation from DGWS's projections

Under condition B of the Licence, the RPI+K price cap limits the annual "weighted average increase" in the standard charges of DCC. This, in turn, is calculated by reference to the "tariff basket formula" (see Chapter 8 under "*Price Control*") 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 in respect of 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, DCC 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. Since actual out-turn revenues are used as the basis for the setting of price limits in the subsequent five year period, any deviation from revenue projections in the previous five year period will be reflected in such price limits.

Optional metering

The UK Water Industry Act 1999 provides for a change in the basis of charging residential customers from unmetered to metered at the election of the customer (see Chapter 8: "*Interim Determination of K*"). This may result in a revenue loss to DCC, although any loss may be ameliorated by the treatment of unmeasured charges in the tariff basket formula used to calculate the annual change in DCC's standard charges. In addition, in 1999 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 determination would be eligible for an Interim Determination (see Chapter 8 under "*Interim Determination of K*"). In September 2000, DCC applied for an Interim Determination in respect of a number of items, including excess meter optants, and, in December 2000, the DGWS increased DCC's price limits for the four years beginning on 1 April 2001 (see Chapter 9 under "*Ofwat's 2000 Interim Determination*" for further details).

However, there is no assurance that such protection would continue to be provided as part of future determinations.

Weather

DCC is 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 Chapter 8 under "*Guaranteed Standards*"). However, DCC's region is one of the least water resource-constrained parts of the country. The last severe drought was in 1996, and it cost DCC £3.5m in reinforcement costs.

Certain Legal Considerations

Security

DCC's ability to provide security for its obligations (including its obligations to the Issuer under the Intercompany Loan Agreements), and the ability to perfect and enforce such security, are each limited by its Licence, the requirements thereunder and the WIA. The vast majority of DCC's assets by value is tangible property which is protected land and/or required for the operation of DCC's business and therefore cannot be effectively secured. In particular, there is no right 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 to block the appointment of an administrator under the UK Insolvency Act 1986.

There are also certain legal restrictions which arise under the WIA and the Licence affecting the enforcement of the security created under the DCC Security. 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 (see Chapter 8 under "*Security*").

Accordingly, the security provided over the assets of DCC to the DCC Secured Creditors, and, therefore, the security available to be secured by the Issuer in favour of the Issuer Secured Creditors in respect of the Issuer's obligations under the Bonds, affords significantly less protection to the DCC Secured Creditors, and hence the Issuer Secured Creditors, than would be the case if DCC 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 Guarantor Security. The enforcement of security over the shares in any company in the Financing Group, including any holding company of DCC, would not be subject to the moratorium set out in the WIA nor would it be an event which would itself result in the making of the special administration order. However, it is anticipated that any intended enforcement directly or indirectly of the Guarantor Security or the security over, and subsequently any planned disposal of, the shares in DCC would require consultation with the DGWS.

Notice of the creation of the DCC Security will not be given initially to DCC's customers or to DCC's contractual counterparties in respect of its contracts (other than certain material contracts). In addition, each charge over DCC's land as purported to be granted will take effect in equity only. Accordingly, until any such assignment is perfected, registration effected with HM Land Registry in respect of registered land or certain other action is taken in respect of unregistered land, any such assignment or charge may be or become subject to prior equities arising (such as rights of set off).

Special Administration

The WIA contains provisions enabling the Assembly and the DGWS 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 DCC 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 DCC to the Court for the winding up of DCC might result in the appointment of a special administrator.

During the period of the special administration order, DCC has to be managed by the special administrator for the purposes of the order and in a manner which protects the interests of members and creditors. Whilst the order is in force, no steps may be taken to enforce any security over DCC's property except with the consent of the special administrator or the leave of the Court. A special administrator would be able to dispose of assets free of any floating charge existing in relation to them. On such a disposal, however, the proceeds would be treated as if subject to a floating charge which has the same priority as that afforded to the original security. A special administrator may not dispose of property which is the subject of a fixed charge without the agreement of the relevant creditor except under an order of the Court. On such a disposal, the special administrator must account for the proceeds to the chargee, although the disposal proceeds to which the chargee is entitled are 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 UK Insolvency Act 1986.

The purposes of a special administration order consist of: (i) transferring to one or more different Regulated 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. It would therefore not be open to the special administrator 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 is effected by a transfer scheme which the special administrator puts 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). (See Chapter 8 under ''*Special Administration Orders*''.)

Financial Assistance

The entry into the Holdings/DCC Loan Agreement will constitute the giving of ''financial assistance'' by DCC within the meaning of Section 151 and 152 of the Companies Act in so far as such financial assistance is given directly or indirectly for the purpose of either (i) assisting the acquisition of shares in DCC by Holdings; or (ii) reducing or discharging liabilities incurred for the purpose of the acquisition of shares in Hyder by WPDL.

However, Sections 155 to 158 of the Companies Act provide an exemption procedure for private companies, which can be used in certain circumstances to approve actions that might otherwise constitute unlawful financial assistance. These provisions require the directors of DCC, HUH and Hyder to make statutory declarations relating to the solvency of DCC, HUH or, as the case may be, Hyder both as at the date on which the assistance is given and for the period of one year immediately following that date and for the financial assistance to be approved by a special resolution of the Hyder shareholders. In addition each of the statutory declarations will have annexed to it a report from the relevant company's auditors stating that they have enquired into the state of affairs of the company and are not aware of anything to indicate that the opinion expressed by the directors in the relevant declaration is unreasonable in all the circumstances. Each of DCC, HUH and Hyder has complied with these provisions in relation to the financial assistance being given by them.

Under section 155(2) of the Companies Act, financial assistance can only be given by DCC, HUH or Hyder if: (i) it has net assets which are not thereby reduced; or (ii) to the extent that its net assets are reduced, if such assistance is provided out of distributable profits. The directors of each of DCC, HUH and Hyder formed the opinion that none of the relevant transactions will result in the reduction in the net assets of such companies, but there can be no assurance that a court or liquidator would concur in this view.

Outsourcing Considerations

As described in Chapter 12 under ''*Procurement and Outsourcing*'', DCC has outsourced the bulk of its day-to-day operations, customer services, maintenance, and capital investment obligations to third parties, under a range of outsourcing contracts. As such, DCC is exposed to a number of additional risks, including: (i) the non-performance or insolvency of, or the abandonment of obligations by, a contractor, and the failure by DCC to secure a replacement contractor in a timely manner following termination of a contract, any of which may cause DCC to breach its obligations under the WIA and Licence; (ii) the possibility that best market prices available for the purposes of any replacement contracts exceed the costs of a previous outsourcing contract, and/or the equivalent amounts assumed by the DGWS at periodic reviews; and (iii) that DCC may breach any of its obligations under any outsourcing contract which would expose it to potentially uncapped liabilities.

However, DCC will be obliged at all times to comply with its Procurement Plan (see Chapter 12: ''*Procurement and Outsourcing*'') and its Outsourcing Policy (see Chapter 4 under ''*Common Terms Agreement*''), under which it will be required to pursue procurement policies designed, *inter alia*, to minimise and mitigate the above risks.

Environmental Considerations

DCC'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 EA as described in Chapter 8: "*Water Regulation*".

Whilst DCC believes that it is in material compliance with all such laws and regulations, there can be no assurance that it will not in future incur significant costs to comply with upgrading requirements imposed under existing or future laws and regulations. Although the costs of such 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 DCC and/or the interests of the Bondholders.

Given the nature of DCC's operations there is a risk that pollution incidents may occur, the possible consequences of which may be criminal prosecution leading to the imposition of fines on DCC 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. The imposition of fines, civil liability, clean up costs or upgrade may materially and adversely affect the financial position of DCC. Any such incidents may also give rise to breaches of any operational environmental permits held by DCC. There is also a risk that DCC may incur liability to clean up contamination caused by historical activities at its sites, whether or not DCC caused the contamination in question. The costs of cleaning up contamination of land and/or water may be significant.

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 DCC's water or sewage treatment works, pumping stations, water mains, sewers or service pipes. Any resulting suspension of operations of DCC could have a material adverse effect on the ability of DCC to meet its financing obligations.

Although the Common Terms Agreement requires DCC to maintain insurance (including business interruption insurance) to protect against certain of these risks, the proceeds of such insurance may not be adequate to cover reduced revenues, increased expenses or other losses or liabilities arising from the occurrence of any of the events described above. Moreover, there can be no assurance that such insurance coverage will be available in the future at commercially reasonable rates. See Chapter 9 under "*DCC-Insurance*".

Glas

As a company limited by guarantee, Glas operates on a not-for-profit basis. It does not have shareholders but, instead, has members who do not receive dividends and, other than their liability to pay £1 on a winding up of the company, have no financial interest in the company. Although measures such as: (i) the proposed changes to the Licence which are, *inter alia*, intended to ensure strict standards of corporate governance, (ii) the performance monitoring regime imposed by Ofwat and, in particular, the use by it of comparative tables of performance in respect of Regulated Companies, (iii) the public adoption by Glas of a member selection policy, (iv) remuneration incentives for senior management of DCC linked, in part, to the performance of DCC and (v) the monitoring of DCC provided under the DCC Transaction Documents, will mitigate any such risk, the lack of financial incentives on the members to ensure efficient management of DCC may mean that, in the absence of shareholders, there may still be risk of insufficient pressure on the management of Glas and DCC to perform to the standard expected of shareholder-owned companies to some extent.

Future Financing

The Issuer will need to raise further debt from time to time in order to finance future capital enhancements to DCC'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 Issuer Payment Date on which principal is required to be repaid, and on the Expected Maturity Date of the relevant Class of Bonds, to refinance the Bonds. Whilst the Issuer STID and other Issuer Transaction Documents contemplate 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 these circumstances, funds will be applied by the Issuer in accordance with the Issuer Pre-Enforcement Payments Priorities or the Issuer Post-Enforcement Payments Priorities, as the case may be.

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 be one that retains the flexibility to respond to changing market conditions, and holds 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, if the DGWS took the view that such debt had not been prudently incurred. However, the DGWS has also stated that he will use the same weighted average cost of capital to determine allowable returns for DCC as is applied to the rest of the sector. Any unfunded costs associated with fixed rate debt would therefore be offset by the fact that DCC's allowable return would include the assumed cost of equity applied to a portion of its regulatory asset value.

Issuer and Bond Considerations

Special Purpose Vehicle Issuer

The Issuer is a special purpose financing entity with no business operations other than the issuance of the Bonds, the lending of the proceeds to DCC under the Intercompany Loan Agreements, loans from Authorised Lenders to the Issuer and the entry into of certain ancillary arrangements. After the Initial Issue Date, other than the proceeds of the issuance of additional Series of Bonds, facilities available from the Liquidity Facility Providers, loans from the Authorised Lenders and funds available from the Hedge Counterparties, the Issuer's principal source of funds will be pursuant to the Intercompany Loan Agreements and the DCC Security. Therefore, the Issuer is subject to all the risks relating to revenues to which DCC is subject, to the extent that such risks could limit funds available to DCC to enable it to satisfy in full and on a timely basis its obligations under the Intercompany Loan Agreements. (See "*Revenue Risks*" above.)

Source of Payments to Bondholders

Although the Class A Bonds will have the benefit of the relevant Bond Policies, none of the Bonds of any Class will be obligations or responsibilities of, nor will they be guaranteed by, any of the Other Parties or any member of the Glas Group (except the Guarantors in relation to DCC but it should be noted in respect of the Guarantors that it is not expected that any of them will own any significant assets other than their direct or indirect interest in the shares of DCC). None of these persons accepts any liability whatsoever in respect of any failure by the Issuer to make any payment of any amount due on the Bonds.

In addition, a Financial Guarantor will guarantee to the relevant Class A Bondholders only the payment of scheduled principal and interest; it will not guarantee any amounts which may be accelerated or any additional amounts (including any Subordinated Coupon Amounts).

Class R Underwriter Non-Performance

If any Class R Bonds are sold by the Issuer (other than on the Initial Issue Date), then under the terms and conditions of the Class R Bonds, the Issuer is obliged (unless there is a subsisting Issuer Event of Default under the Bonds) to re-purchase all Class R Bonds so sold (or which have previously been sold) from the holders thereof on the immediately following Issuer Payment Date. The funds necessary to complete such re-purchase may be raised in a number of ways, including the application of the proceeds of a repayment or prepayment of one or more of the Revolving Advances of the Intercompany Loan, the issue of a further Series of Bonds, or the resale of Class R Bonds (which may include the Class R Bonds being re-purchased).

If a re-purchase of Class R Bonds is being financed through the resale of Class R Bonds, the Issuer may not have sufficient resources to meet its obligation to re-purchase such Class R Bonds if any Class R Underwriter fails to agree to purchase the Class R Bonds being so resold up to and including 31 March 2006. However, any Class R Bonds not repurchased due to such a failure will continue to bear interest and will be capable (to the extent the Issuer has funds available on a subsequent Issuer Payment Date) of being repurchased by the Issuer on a subsequent Issuer Payment Date. However, there can be no assurance that the Issuer will have sufficient funds on a subsequent Issuer Payment Date to repurchase such Class R Bonds in any event and this may lead, ultimately, to an Issuer Event of Default arising in respect of the Bonds.

Subordination of Class C Bonds and Class D Bonds

The Class A Bonds, Class B Bonds and Class R Bonds (each of whatever Sub-Class) will rank in priority to payments of principal and interest due on all Sub-Classes of the Class C Bonds. The Class A Bonds, Class B Bonds, Class R Bonds and Class C Bonds (each of whatever Sub-Class) will rank in priority to payments of principal and interest due on all Sub-Classes of the Class D Bonds.

If, on any Issuer Payment Date, prior to delivery of an enforcement notice there are insufficient funds available to the Issuer to pay accrued interest on the Class C Bonds and/or Class D Bonds, the Issuer's liability to pay such accrued interest will be treated as not having fallen due and should be deferred until the earlier of (i) the next following Issuer Payment Date on which the Issuer has, in accordance with the Issuer Pre-Enforcement of Payments Priorities, sufficient funds available to pay such deferred amounts (including any interest accrued thereon); and (ii) the Issuer Payment Date of the last maturing Bond which ranks in priority to the Class C Bonds or the Class D Bonds, as the case may be. Interest will, however, accrue on such deferred interest.

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

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 set out in Chapter 4 under "*Hedging Agreements*", including where the Hedge Counterparty or the Issuer is respectively required to gross up for payments of tax that have been required to be deducted or withheld by law, which requirement has not been able to be avoided, notwithstanding the Issuer and the Hedge Counterparty having used reasonable endeavours so to do. 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, as a result of making any termination payment to the Hedge Counterparty, which payment will be in accordance with the Issuer Pre-Enforcement Payments Priorities or the Issuer Post-Enforcement Payments Priorities as the case may be. (See Chapter 4 under "*Issuer Cash Management*".)

The Liquidity Facilities

The Liquidity Facility Agreements are intended to cover shortfalls of interest on the Class A Bonds, Class B Bonds, Class R Bonds and (subject to certain limits) Class C Bonds, as well as senior interest payments on any Authorised Loan Facility and scheduled interest payments on the Finance Leases that arise on any Issuer Payment Date or DCC Payment Date, as the case may be. The Liquidity Facilities will not be available to meet any such shortfalls in respect of the Class D Bonds. However, on any such Issuer Payment Date, there are no assurances that any such shortfalls will be met in whole or in part by the Liquidity Facility Agreements, thereby having an effect on the payments to be made, *inter alia*, in respect of the Bonds.

Rights Available to Bondholders

The Trust Deed contains provisions detailing the Bond Trustee's obligations to consider the interests of the Bondholders as regards all powers, trusts, authorities, duties and discretions of the Bond Trustee (except where expressly provided otherwise). In particular, subject as provided in the following sentence, the Bond Trustee will consider the interests of the holders of the Most Senior Class of Bonds (as defined in the Conditions) 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 Sub-Classes of such Bonds, it shall consider the interests of the holders of the Sub-Class of the Most Senior Class of Bonds then outstanding with the shortest dated maturity. To the extent that the exercise of any rights, powers, trusts and discretions of the Bond Trustee affects or relates to any Class A Bonds, the Bond Trustee shall only act with the consent of the relevant Financial Guarantor(s) in accordance with the Issuer STID. The Issuer STID provides that the Issuer Security Trustee (except in relation to its reserved matters and entrenched rights) will act on instructions of the Issuer Instructing Group. When so doing,

the Issuer Security Trustee is not required to have regard to the interests of any Issuer Secured Creditor (including the Bond Trustee as trustee for the Bondholders) in relation to the exercise of such rights and, consequently, has no liability to the Bondholders as a consequence of so acting.

Intercreditor Rights of Bondholders

The right to instruct the Issuer Security Trustee, *inter alia*, to direct the exercise and enforcement of the Issuer's rights under the DCC Transaction Documents and Issuer Transaction Documents and to give consents and waivers thereunder is restricted to the Issuer Instructing Group. Prior to a Default Situation, broadly, only the Financial Guarantors of Class A Bonds (for so long as there are Class A Bonds outstanding in respect of which no FG Event of Default has occurred in respect of the relevant Financial Guarantor and provided that amounts could still become payable by the Issuer to the relevant Financial Guarantor under the Issuer Transaction Documents) and any facility agent or single lender under an Authorised Loan Facility (for so long as the relevant loan amount remains outstanding) will be entitled to comprise the Issuer Instructing Group, provided that such Issuer Qualifying Debt Representatives have provided an indemnity on terms acceptable to the Issuer Security Trustee. The Issuer has covenanted in favour of the Issuer Security Trustee to use its reasonable endeavours to ensure that all times it has an Issuer Qualifying Debt Representative which is a Financial Guarantor in order to ensure that the Issuer Security Trustee can be instructed and can take instructions in a timely manner. Accordingly, prior to a Default Situation and for so long as a Financial Guarantor comprises and remains entitled to comprise the Issuer Instructing Group, the Bondholders of all Sub-Classes will be bound by the actions of the Issuer Security Trustee taken on the instructions of the Issuer Instructing Group. In addition, in response to an Emergency Instruction Notice, the Bond Trustee or the Issuer Security Trustee, as the case may be, may be required to take certain action (as specified in such notice) without reference to the Bondholders (see Chapter 4 under "*Summary of Intercreditor Arrangements*").

In a Default Situation the holders of Class C Bonds and Class D Bonds shall not be entitled to be represented by the Bond Trustee in the Issuer Instructing Group where there is an Issuer Qualifying Debt Representative in respect of any Authorised Loan Facility, the Class A Bonds, the Class B Bonds and the Class R Bonds (and, in the case of holders of Class D Bonds, the Class C Bonds).

Whatever the composition of the Issuer Instructing Group, any decision of the Issuer Instructing Group shall be effective and binding on all Intercreditor Parties at the Issuer level (including all Bondholders). However, no decision of the Issuer Instructing Group shall be effective to the extent that the matter on which the relevant vote or instruction has been given relates to a Basic Terms Modification of any Bonds or to certain entrenched rights and reserved matters of the Issuer Security Trustee or the other Issuer Secured Creditors (including the Bond Trustee).

Limited Liquidity of the Bonds; Absence of Secondary Market for the Bonds

Notwithstanding the fact that an application has been made to list the Bonds on the Luxembourg Stock Exchange, 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, amongst 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 DCC, developments and trends in the water industry generally and events in the licensed territory of DCC.

Rating of the Bonds

The ratings anticipated to be assigned to the Class A Bonds to be issued on the Initial Issue Date are based solely on the debt rating of MBIA and reflect only the views of the Ratings Agencies. The ratings anticipated to be assigned to the Class B Bonds, Class R Bonds and Class C Bonds by the Rating Agencies reflect only the views of the Rating Agencies and are based primarily on the long-term unsecured and unsubordinated debt rating of DCC and also on the other relevant structural features and assets of the transaction. The Class D Bonds will not be rated by 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 DCC or, in the case of the Class A Bonds, of the relevant 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 DCC and/or circumstances relating to the water industry generally, could have an adverse impact on the ratings of the Bonds.

Withholding Tax under the Bonds

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 1 under "*Redemption for Index Event, Taxation or other Reasons*" and Chapter 6 under "*Terms and Conditions of the Bonds*".)

Likewise, in the event withholding taxes are imposed in respect of payments due under the Class A Bonds and the relevant Financial Guarantor is called upon under its Bond Policy or Bond Policies to make payments in respect of such payments, such Financial Guarantor is not obliged to gross-up or otherwise compensate Class A Bondholders for the fact that such Class A 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.

Adoption of Proposed European Directive on the Taxation of Savings

The European Union is currently considering proposals for a new directive regarding the taxation of savings income. Subject to a number of important conditions being met, it is proposed that a Member State will be required to provide to the tax authorities of another Member State details of payments of interest or other similar income paid by a person within its jurisdiction to an individual resident in that other Member State, subject to the right of certain Member States to opt instead for a withholding system for a transitional period in relation to such payments. The proposals are not yet final, and they may be subject to further amendment and clarification.

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 Initial Issue Date which change might impact on the Bonds and the expected payments of interest and repayment of principal.

European Monetary Union

Prior to the maturity of the Bonds, the United Kingdom may become a participating member state in the Economic and Monetary Union and the euro may become the lawful currency of the United Kingdom. Adoption of the euro by the United Kingdom 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. (See Chapter 6: "*The Bonds – Terms and Conditions 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.

Financial Projections of DCC

The financial projections set out in Chapter 9 under "*Financial Projections of DCC*" have been prepared for illustrative purposes only. Actual events and circumstances may vary from the assumptions made, perhaps materially. No representation is made or intended, nor should any be inferred, with respect to the likely occurrence or existence of any particular fact or circumstance. If facts or circumstances occur which are less favourable than those projected, or if the assumptions used in formulating the financial projections prove to be incorrect, DCC may be unable to satisfy its obligations under, *inter alia*, the Intercompany Loan Agreements, which may result in turn in the Issuer being unable to meet its obligations under the Bonds.

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 of any Sub-Class, or the inability of a Financial Guarantor to pay scheduled interest or repay scheduled principal on the Class A 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 of any Sub-Class receive payment of interest or repayment of principal from the Issuer in respect of such Bonds, or from a Financial Guarantor in respect of the Class A Bonds, on a timely basis or at all.

CHAPTER 6

THE BONDS

TERMS AND CONDITIONS OF THE BONDS

The following is the text of the terms and conditions which (subject to completion and amendment and as supplemented or varied in accordance with the provisions of the relevant Pricing Supplement and, save for the italicised paragraphs) will be incorporated by reference into each Global Bond representing Bonds in bearer form, Bond in definitive form (if any) issued in exchange for the Global Bond(s) representing Bonds in bearer form, Regulation S Global Registered Bond Certificate representing Bonds in registered form and Regulation S Individual Registered Bond Certificate representing Bonds in registered form (only if such incorporation by reference is permitted by the relevant stock exchange and agreed by the Issuer). If such incorporation by reference is not so permitted and agreed, each Bond in bearer form and each Regulation S Individual Registered Bond Certificate representing Bonds in registered form will have endorsed thereon or attached thereto such text (as so completed, amended, varied or supplemented). Further information with respect to each Sub-Class of Bonds will be given in the relevant Pricing Supplement which will provide for those aspects of these Conditions which are applicable to such Sub-Class of Bonds, including, in the case of Class A Bonds, the form of Bond Policy and endorsement and, in the case of all Classes, the terms of the relevant Term Advance or Revolving Advance under the relevant Intercompany Loan Agreement. References in the Conditions to "Bonds" are, as the context requires, references to the Bonds of one Sub-Class only, not to all Bonds which may be issued under the Programme.

The Issuer will issue bonds pursuant to a trust deed dated on or about 10 May 2001 (the "**Initial Issue Date**") (as amended, supplemented, restated and/or novated from time to time, the "**Trust Deed**") between Dwr Cymru (Financing) Limited (the "**Issuer**"), MBIA Assurance S.A. ("**MBIA**"), any other Financial Guarantor (as defined below) acceding thereto and Bankers Trustee Company Limited as trustee (the "**Bond Trustee**", which expression includes the trustee or trustees for the time being of the Trust Deed).

The Class A Bonds (as defined in Condition 1(a) below) alone will be unconditionally and irrevocably guaranteed as to scheduled payments of principal and interest (as adjusted for indexation but excluding any accelerated amounts or amounts by which the Coupons (as defined below) exceed the Initial Coupons on such Sub-Class as at the relevant Issue Date (the "**Subordinated Coupon Amounts**")) in respect of such Class A 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 each Sub-Class (as defined in Condition 1(a) below) of Class A Bonds.

None of the Class B Bonds, Class R Bonds, Class C Bonds or Class D Bonds (each as defined in Condition 1(a) below) will have the benefit of any such Bond Policy.

The Bonds will have the benefit (to the extent applicable) of an agency agreement (as amended, supplemented and/or restated from time to time, the "**Paying Agency Agreement**") dated the Initial Issue Date (as to which the Issuer, the Bond Trustee, the Principal Paying Agent and the other Paying Agents (in the case of Bearer Bonds) and the Transfer Agents and the Registrar (in the case of Registered Bonds) are party). As used herein, each of "**Principal Paying Agent**", "**Paying Agents**", "**Transfer Agents**" and/or "**Registrar**" means, in relation to the Bonds, the persons specified below relating to the Bonds as the Principal Paying Agent, Paying Agents, Transfer Agents and/or Registrar, respectively, and, in each case, any successor to such person in such capacity.

The relevant Pricing Supplement relating to the Bonds will be endorsed upon or attached to the Bonds and will supplement these terms and conditions (the "**Conditions**") and may specify other terms and conditions which shall, to the extent so specified or to the extent inconsistent with these Conditions, replace or modify these Conditions for the purpose of the Bonds.

On the Initial Issue Date, the Issuer entered into a deed of charge (the "**Issuer Deed of Charge**") with Bankers Trustee Company Limited as security trustee (the "**Issuer Security Trustee**"), pursuant to which the Issuer granted certain fixed and floating charge security (the "**Issuer Security**") to the Issuer Security Trustee for itself and on behalf of the Bond Trustee (for itself and on behalf of the Bond holders), the Financial Guarantor(s), the Liquidity Facility Providers, the Hedge Counterparties,

the Account Bank, the Authorised Lenders, the Paying Agents, the Registrar, the Transfer Agents, the Cash Manager (each as defined therein), any receiver and any additional creditor of the Issuer which accedes to the Issuer STID (as defined below) (together, the "**Issuer Secured Creditors**").

On the Initial Issue Date, the Issuer entered into a security trust and intercreditor deed (the "**Issuer STID**") with the Issuer Security Trustee and other Issuer Secured Creditors, pursuant to which the Issuer Security Trustee holds the Issuer Security on trust for the Issuer Secured Creditors and the Issuer Secured Creditors agree to certain intercreditor arrangements.

The Issuer has entered or may enter into a dealership agreement (together, the "**Dealership Agreements**") with the dealers named therein (the "**Dealers**") in respect of each Sub-Class of Bonds issued by the Issuer, pursuant to which the Dealers have agreed to purchase the relevant Sub-Class of Bonds on behalf of the Issuer.

On the Initial Issue Date, the Issuer entered into an underwriting agreement (the "**Class R Underwriting Agreement**") with the underwriters named therein (the "**Class R Underwriters**") pursuant to which the Class R Underwriters agreed to underwrite the sale of the Class R Bonds.

On the Initial Issue Date, the Issuer entered into a master framework agreement (the "**Master Framework Agreement**") with the Issuer Security Trustee for itself and on behalf of the Issuer Secured Creditors, which contains certain representations, warranties and covenants of the Issuer.

The Issuer has entered or may enter into liquidity facility agreements (together, the "**Liquidity Facility Agreements**") with certain liquidity facility providers (together, the "**Liquidity Facility Providers**") in respect of each Series of Bonds issued by the Issuer, pursuant to which the Liquidity Facility Providers agree to make certain facilities available to meet liquidity shortfalls.

The Issuer has entered or may enter into certain revolving credit facilities (together, the "**Authorised Loan Facilities**") with certain lenders (the "**Authorised Lenders**"), pursuant to which the Authorised Lenders agree to make certain facilities available to the Issuer for the purpose of funding certain working capital, capital expenditure and other expenses of DCC.

The Issuer has entered or may enter into certain currency and interest-rate hedging agreements (together, the "**Hedging Agreements**") with certain hedge counterparties (together, the "**Hedge Counterparties**") in respect of certain Sub-Classes of Bonds, pursuant to which the Issuer hedges certain of its currency and interest-rate obligations.

The Trust Deed, the Issuer Deed of Charge, the Issuer STID, the Paying Agency Agreement, the Dealership Agreements, the Class R Underwriting Agreement, the Pricing Supplements, the Liquidity Facility Agreements, the Hedging Agreements, the Authorised Loan Facilities, the Intercompany Loan Agreements (as defined below), the Insurance and Indemnity Agreements (as defined below) and the Master Framework Agreement are together referred to as the "**Issuer Transaction Documents**".

Certain statements in these Conditions are summaries of the detailed provisions in the relevant Pricing Supplement or in the Trust Deed, the Issuer Deed of Charge or the Issuer STID. Copies of, *inter alia*, the Trust Deed, the Issuer Deed of Charge, the Issuer STID, the relevant Pricing Supplement, the Paying Agency Agreement, the Dealership Agreements, the Class R Underwriting Agreement, the Liquidity Facility Agreements, the Authorised Loan Facilities, the Hedging Agreements, the Insurance and Indemnity Agreements, the Intercompany Loan Agreements and the Master Framework Agreement are available for inspection at the specified offices of the Principal Paying Agent or the Paying Agents (in the case of bearer Bonds) or the specified offices of the Transfer Agents and the Registrar (in the case of registered Bonds).

The Bondholders (as defined in Condition 1(c) below) are entitled to the benefit of, are bound by, and are deemed to have notice of, all the provisions of the Trust Deed, the Issuer Deed of Charge, the Issuer STID, the Master Framework Agreement and the relevant Pricing Supplement and to have notice of those provisions of the Paying Agency Agreement and the other Issuer Transaction Documents applicable to them.

Any reference in these conditions to a matter being "specified" means as the same may be specified in the relevant Pricing Supplement.

1. Classes, Form, Denomination and Title

(a) Classes and Sub-Classes of Bonds

Bonds issued on the same Issue Date (as defined in Condition 6(i)) comprise a series (each a "**Series**" (as specified in the relevant Pricing Supplement)). Each Series comprises one or more classes of Bonds (each a "**Class**"). The available Classes of Bonds will be "**Class A Bonds**", "**Class B Bonds**", "**Class R Bonds**", "**Class C Bonds**" and "**Class D Bonds**". Each Class of Bonds will be further sub-divided into non-fungible sub-classes (each a "**Sub-Class**" (as specified in the relevant Pricing Supplement)) of Bonds, with each Sub-Class being denominated in different specified currencies or having different Aggregate Nominal Amounts, Interest Rates, Maturity Dates, Issue Prices or other terms (as specified in the relevant Pricing Supplement).

Bonds of any Sub-Class may be fixed rate ("**Fixed Rate Bonds**"), floating rate ("**Floating Rate Bonds**") or index-linked including limited indexed ("**Indexed Bonds**"), depending on the method of calculating interest payable in respect of such Bonds.

(b) Form and Denomination

The Bonds will be issued either (i) in bearer form ("**Bearer Bonds**"), serially numbered in a Specified Denomination (as specified in the relevant Pricing Supplement) or an integral multiple thereof, or (ii) in registered form ("**Registered Bonds**") serially numbered in a Specified Denomination or an integral multiple thereof. References in these Conditions to "**Bonds**" include Bearer Bonds and Registered Bonds and, where the context requires, Bonds of all Sub-Classes, Classes and Series.

Interest-bearing Bearer Bonds are issued with Coupons (and, where appropriate, a Talon) attached. After all the Coupons attached to, or issued in respect of, any Bearer Bond which was issued with a Talon have matured, a coupon sheet comprising further Coupons (other than Coupons which would be void) and (if necessary) one further Talon will be issued against presentation of the relevant Talon at the specified office of any Paying Agent. Any Bearer Bond the principal amount of which is redeemable in instalments may be issued with one or more Receipts attached thereto.

"**Maturity Date**" means the date specified in the relevant Pricing Supplement as the final date on which the principal amount of the Bond is due and payable.

A Regulation S Individual Registered Bond Certificate (a "**Registered Bond Certificate**") substantially in the form of Schedule 3, Part B to the Trust Deed will be issued to each Bondholder in respect of its registered holding.

(c) Title

Title to Bearer Bonds, Coupons, Receipts and Talons (if any) passes by delivery. Title to Registered Bonds passes by registration in the register (the "**Register**"), which the Issuer shall procure to be kept by the Registrar.

In these Conditions, subject as provided below, each of "**Bondholder**" (in relation to a Bond, Coupon, Receipt or Talon), "**holder**" and "**Holder**" means (i) in relation to a Bearer Bond, the bearer of any Bearer Bond, Coupon, Receipt or Talon (as the case may be) and (ii) in relation to Registered Bond, the person in whose name a Registered Bond is registered, as the case may be. The expressions "Bondholder", "holder" and "Holder" include the holders of instalment receipts (the "**Receipts**") appertaining to the payment of principal by instalments (if any) attached to such Bonds in bearer form (the "**Receiptholders**") and the holders of the coupons (the "**Coupons**") (if any) appertaining to interest bearing Bonds in bearer form (the "**Couponholders**", which expression includes the holders of talons (the "**Talons**") (if any) for further coupons attached to such Bonds (the "**Talonholders**")).

The holder of any Bond, Coupon, Receipt or Talon will (except as otherwise required by law) be treated as its absolute owner for all purposes (whether or not it is overdue and regardless of any notice of ownership, trust or any interest in it, any writing on the relevant Bond or Registered Bond Certificate, or its theft or loss or any express or constructive notice of any claim by any other person of any interest therein other than, in the case of a Registered Bond, a duly executed transfer of such Bond in the form endorsed on the Registered Bond Certificate in respect thereof) and no person will be liable for so treating the holder.

(d) Fungible Issues of Bonds comprising a Sub-Class

A Sub-Class of Bonds may comprise a number of issues in addition to the initial Series of such Sub-Class, each of which will be issued on identical terms save for the first interest payment. Such further issues of the same Sub-Class will be fungible with the prior issue.

2. Exchanges of Bearer Bonds for Registered Bonds and Transfers of Registered Bonds

(a) Exchange of Bonds

Subject to Condition 2(e), Bearer Bonds may, if so specified in the relevant Pricing Supplement, be exchanged at the expense of the transferor Bondholder for the same aggregate principal amount of Registered Bonds at the request in writing of the relevant Bondholder and upon surrender of the Bearer Bond to be exchanged together with all unmatured Coupons, Receipts and Talons (if any) relating to it at the specified office of the Registrar or any Transfer Agent or Paying Agent. Where, however, a Bearer Bond is surrendered for exchange after the Record Date (as defined in Condition 9(b)) for any payment of interest or Interest Amount (as defined in Condition 6(h)), the Coupon in respect of that payment of interest or Interest Amount need not be surrendered with it.

Registered Bonds may not be exchanged for Bearer Bonds.

(b) Transfer of Registered Bonds

A Registered Bond may be transferred upon the surrender of the relevant Registered Bond Certificate, together with the form of transfer endorsed on it duly completed and executed, at the specified office of any Transfer Agent or the Registrar. However, a Registered Bond may not be transferred unless (i) the principal amount of Registered Bonds proposed to be transferred and (ii) the principal amount of the Registered Bonds proposed to be the principal amount of the balance of Registered Bonds to be retained by the relevant transferor are, in each case, Authorised Denominations. In the case of a transfer of part only of a holding of Registered Bonds represented by a Registered Bond Certificate, a new Registered Bond Certificate in respect of the balance not transferred will be issued to the transferor within three business days (in the place of the specified office of the Transfer Agent or the Registrar) of receipt of such form of transfer.

(c) Delivery of New Registered Bond Certificates

Each new Registered Bond Certificate to be issued upon exchange of Bearer Bonds or transfer of Registered Bonds will, within three business days (in the place of the specified office of the Transfer Agent or the Registrar) of receipt of such request for exchange or form of transfer, be available for delivery at the specified office of the Transfer Agent or the Registrar stipulated in the request for exchange or form of transfer, or be mailed at the risk of the Bondholder entitled to the Registered Bond Certificate to such address as may be specified in such request or form of transfer. For these purposes, a request for exchange or form of transfer received by the Registrar after the Record Date in respect of any payment due in respect of Registered Bonds shall be deemed not to be effectively received by the Registrar until the business day following the due date for such payment.

(d) Exchange at the Expense of Transferor Bondholder

Registration of Bonds on exchange or transfer will be effected at the expense of the transferor Bondholder by or on behalf of the Issuer, the Transfer Agent or the Registrar, and upon payment of (or the giving of such indemnity as the Transfer Agent or the Registrar may require in respect of) any tax or other governmental charges which may be imposed in relation to it.

(e) Closed Periods

No transfer of a Registered Bond to be registered, nor exchange of a Bearer Bond for a Registered Bond may occur during the period of 15 days ending on the due date for any payment of principal, interest, Interest Amount or Redemption Amount (as defined in Condition 6(i) below) on that Bond.

3. Status of Bonds and Bond Policy

(a) Status of Class A Bonds, Class B Bonds and Class R Bonds

This Condition 3(a) is applicable only in relation to Bonds which are specified as being a Sub-Class of Class A Bonds, Class B Bonds or Class R Bonds.

The Bonds, Coupons, Talons and Receipts (if any) are direct and unconditional obligations of the Issuer, secured in the manner described in Condition 4 and will rank *pari passu* without any preference among themselves. However, the Class B Bonds and the Class R Bonds will not have the benefit of any Bond Policy.

(b) Status of Class C Bonds

This Condition 3(b) is applicable only in relation to Bonds which are specified as being a Sub-Class of Class C Bonds.

The Bonds, Coupons, Talons and Receipts (if any) are direct and unconditional obligations of the Issuer, are secured in the manner described in Condition 4, are subordinated to the Class A Bonds, Class B Bonds and Class R Bonds and rank *pari passu* without any preference among themselves.

(c) Status of Class D Bonds

This Condition 3(c) is applicable only in relation to Bonds which are specified as being a Sub-Class of Class D Bonds.

The Bonds, Coupons, Talons and Receipts (if any) are direct and unconditional obligations of the Issuer, are secured in the manner described in Condition 4, are subordinated to the Class A Bonds, Class B Bonds, Class R Bonds and Class C Bonds and rank *pari passu* without any preference among themselves.

(d) Bond Policy Issued by Financial Guarantor

This Condition 3(d) is applicable only in relation to Bonds which are specified as being a Sub-Class of Class A Bonds.

Class A Bonds will have the benefit of a Bond Policy issued by a Financial Guarantor specified in the relevant Pricing Supplement, issued pursuant to an insurance and indemnity agreement between the Issuer and the relevant Financial Guarantor dated on or before the relevant Issue Date (as defined in Condition 6(i)) of such Bonds (each an "**Insurance and Indemnity Agreement**"). Under the relevant Bond Policy, the relevant Financial Guarantor unconditionally and irrevocably agrees to pay to the Bond Trustee all sums due and payable but unpaid by the Issuer in respect of scheduled interest (adjusted for indexation in accordance with these Conditions but not any Subordinated Coupon Amounts) and payment of principal (but not any accelerated amounts) on such Class A 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 the relevant Scheduled Payment Date (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 so to do 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 payable but on the basis that amounts paid by the Issuer in respect of principal would be applied to reduce the relevant Financial Guarantor's obligations *pari passu* in inverse order of maturity.

To the extent that the early redemption price of any Bonds exceeds the aggregate of the Principal Amount Outstanding of and any accrued interest outstanding on any such Bonds to be redeemed, payment of such early redemption price 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 a Sub-Class of Class A Bonds.

The relevant Bond Policy provided by the relevant Financial Guarantor in respect of the Bonds will constitute a direct, unsecured obligation of the relevant Financial Guarantor which will rank at least *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.

(f) Class R Underwriting Agreement

This Condition 3(f) is applicable only in relation to Bonds which are specified as being a Sub-Class of Class R Bonds.

During the Underwriting Period (as defined in Condition 8(e)(vii)), the Issuer will have the benefit of the Class R Underwriting Agreement. Under the Class R Underwriting Agreement, the Class R Underwriters (as defined in Condition 8(e)(vii)) may agree to purchase, subject to certain conditions, Class R Bonds in an aggregate principal amount not exceeding £100,000,000 from the Issuer. The Class R Underwriting Agreement also sets out the terms on which the Class R Underwriters can novate their underwriting commitments and also contains certain warranties and indemnities given to the Class R Underwriters by the Issuer.

(g) Related Agreements

The primary asset of the Issuer will be its rights against Dŵr Cymru Cyfyngedig (an affiliate of the Issuer) ("**DCC**") under the intercompany loan agreements (the "**Intercompany Loan Agreements**") to be entered into by the Issuer with DCC, in respect of which the Issuer will have the benefit of certain security granted by DCC (the "**DCC Security**") and the benefit of certain guarantees and related security granted by affiliates of DCC (the "**Guarantor Security**"). Certain terms of the relevant Intercompany Loan Agreement relating to the Series of Bonds are specified in the relevant Pricing Supplement.

(h) Issuer Security Trustee not responsible for monitoring compliance

As a consequence of the assignment by the Issuer in the Issuer Deed of Charge of the Issuer's rights under the Intercompany Loan Agreements, the Issuer Security Trustee will have all the rights of the Issuer thereunder (except as provided in the Issuer STID and the Issuer Deed of Charge) which rights it will exercise in accordance with the directions of the Issuer Instructing Group. The Issuer Security Trustee shall not be responsible for monitoring compliance by DCC with its obligations under the Intercompany Loan Agreements and the other DCC Transaction Documents (as defined in the Master Framework Agreement) except by means of receipt from DCC of certificates of compliance pursuant to the provisions of the Intercompany Loan Agreements. In particular, where a DCC Event of Default, representation or warranty refers to Material Adverse Effect, material adverse change, materiality or like terminology, the Issuer Security Trustee will not determine such matters (or the absence thereof). DCC has, in the Intercompany Loan Agreement, covenanted with and undertaken to deliver to the Issuer Security Trustee certificates stating whether or not such obligations have been complied with (and whether a DCC Event of Default or potential DCC Event of Default has occurred) and giving details of any non-compliance. The Issuer Security Trustee shall be entitled to rely on such certificates absolutely unless it is instructed otherwise by the Issuer Instructing Group, in which case it will be bound to act on such instructions in accordance with the Issuer STID. Where the Issuer Instructing Group consists of the Bond Trustee acting on behalf of the relevant Bondholders as referred to in the Issuer STID, the Bond Trustee will not determine Material Adverse Effect, material adverse change, materiality or like terminology, but will instead seek that such determination be made by such relevant Bondholders by means of an Extraordinary Resolution.

All Bondholders shall be entitled to a copy of the Periodic Information (as defined in the Master Framework Agreement) as and when available and to a copy of the unaudited interim accounts and audited annual accounts of DCC within 90 days of 30 September and 31 March, respectively. The information referred to in this paragraph is publicly available information, in contrast to the Company Information and the Investors' Report (each as defined below). Such Periodic Information and such accounts will be made available to Bondholders on the website of Glas Cymru Cyfyngedig ("**Glas**").

All DCC Secured Creditors and Issuer Secured Creditors (including the Bondholders) shall be entitled to a copy of the Investors' Report (as defined in the Master Framework Agreement) produced by DCC within 45 days of each of 31 March and 30 September and within 60 days of each of 30 June and 31 December. Such Investors' Report will be made available to Bondholders on a secure part of the Glas website, with the password to such part of the website being provided to the Bondholders (whenever the Investors' Report is produced) in accordance with Condition 17 (although no such notice shall be required to be published in a newspaper). Any Bondholder who provides sufficient evidence of identity may obtain the current password upon application to the Principal Paying Agent or the Registrar (as applicable).

In addition, DCC has covenanted to provide the DCC Secured Creditors and Issuer Secured Creditors who are entitled to vote in accordance with the DCC STID or the Issuer STID, as the case may be, with detailed information on its performance (the "**Company Information**"), as a consequence of which it is possible that the Issuer Instructing Group may direct the Issuer Security Trustee to take action in relation to DCC. After a Default Situation (as defined in the Master Framework Agreement), or where the relevant Financial Guarantor (as defined in the Master Framework Agreement) is not the Issuer Qualifying Debt Representative (as defined in the Master Framework Agreement) for the Class A Bonds, or where there is no Qualifying Debt (as defined in the Master Framework Agreement) in paragraphs (i) and (ii) of the definition thereof, the Bondholders will also be entitled to have access to the Company Information through a separate secure area of the Glas website in the same manner as set out above for the Investors' Reports.

In the event of the Glas website at any time becoming non-operational, all such information set out above which would otherwise be available to the Bondholders will be available for inspection at the specified offices of the Paying Agents, the Transfer Agents or the Registrar, as the case may be, and as further specified in the Paying Agency Agreement.

The Bond Trustee, the Issuer Security Trustee, the DCC Security Trustee and the other DCC Secured Creditors and Issuer Secured Creditors will have access to all the information referred to in this Condition 3(h) except that the Bond Trustee will not have access to the Company Information before the Bondholders become entitled to access to it in accordance with this Condition. However, prior to a Default Situation, where the relevant Financial Guarantor is not the Issuer Qualifying Debt Representative for the Class A bonds, and where there is Qualifying Debt in paragraphs (i) and (ii) of the definition thereof none of the Bond Trustee, the Issuer Security Trustee or the DCC Security Trustee will be entitled or obliged to provide the Company Information to Bondholders and (in the case of the Issuer Security Trustee) will not analyse such information but will instead rely on the certifications referred to above.

4. Security, Priority and Relationship with Issuer Secured Creditors

(a) Security

Under the Issuer Deed of Charge, the Bonds are secured by the Issuer Security (including future property) granted by the Issuer in favour of the Issuer Security Trustee (for itself and on behalf of the Issuer Secured Creditors (including the Bond Trustee for itself and on behalf of the Bondholders)). There is no intention to create further security for the benefit of the holders of Bonds issued after the first Series issued by the Issuer. Each further Series of Bonds issued by the Issuer and any additional creditor of the Issuer acceding to the Issuer STID will share in the Issuer Security.

(b) Relationship among Bondholders and with other Issuer Secured Creditors

The Trust Deed contains provisions detailing the Bond Trustee's obligations to consider the interests of the Bondholders as regards all powers, trusts, authorities, duties and discretions of the Bond Trustee (except where expressly provided otherwise and as further referred to in Condition 16(a)).

The Issuer STID provides that the Issuer Security Trustee (except in relation to its Reserved Matters and Entrenched Rights, each as defined in the Issuer STID) will act on instructions of the Issuer Instructing Group (as defined in the Issuer STID) and, when so doing, the Issuer Security Trustee is not required to have regard to the interests of any Issuer Secured Creditor (including the Bond Trustee as trustee for the Bondholders) in relation to the exercise of such rights and, consequently, has no liability to the Bondholders as a consequence of so acting.

(c) Application Prior to Enforcement

Prior to enforcement of the Issuer Security by the Issuer Security Trustee, the Cash Manager, on behalf of the Issuer, is required to apply funds available to the Issuer in accordance with the Issuer Pre-Enforcement Payments Priorities (as set out in the Issuer STID).

(d) Enforceable Security

In the event of the Issuer Security (as defined in the Master Framework Agreement) becoming enforceable as provided in Condition 11, the Issuer Security Trustee shall, if instructed by the Issuer Instructing Group, enforce its rights with respect to the Issuer 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 Issuer Secured Creditor (including the Bond Trustee as trustee for the Bondholders), provided that the Issuer Security Trustee shall not be obliged to take any action unless it is indemnified and/or secured to its satisfaction.

(e) Application After Enforcement

Subject to the provisions of the Issuer Deed of Charge and the Issuer STID and as specified in the relevant Pricing Supplement, after enforcement of the Issuer Security, the Issuer Security Trustee shall (to the extent that such funds are available) use funds standing to the credit of the Issuer Accounts to make payments in accordance with the Issuer Post-Enforcement Payments Priorities (as set out in the Issuer STID). After such enforcement, amounts payable to any receiver, the Issuer Security Trustee and any Financial Guarantor (in respect of the relevant Class A Bonds) and certain amounts payable to other Issuer Secured Creditors will rank in priority to payments on the Bonds, as set out in the Issuer Post-Enforcement Payments Priorities.

(f) Bond Trustee and Issuer Security Trustee not liable for security

The Bond Trustee and the Issuer 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 Issuer Security and held by way of security for the Bonds, and shall not be bound to enquire into or be liable for any defect or failure in the right or title of the Issuer to the Issuer Security whether such defect or failure was known to the Bond Trustee or the Issuer 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 in favour of the Issuer under the DCC Security or the Guarantor Security 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 Issuer 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 Issuer has agreed to comply with the Issuer Covenants as set out in the Master Framework Agreement.

The Bond Trustee shall be entitled to rely absolutely on a certificate of any director of the Issuer in relation to any matter relating to the Issuer Covenants and to accept without liability any such certificate as sufficient evidence of the relevant fact or matter stated in such certificate.

6. Interest and other Calculations

(a) Interest Rate and Accrual

Each Bond bears interest on its Principal Amount Outstanding (or as otherwise specified in the relevant Pricing Supplement) from the Interest Commencement Date (as defined in Condition 6(i)) at the Interest Rate (as defined in Condition 6(i)), such interest being payable in arrear (unless otherwise specified in the relevant Pricing Supplement) on each Interest Payment Date (as defined in Condition 6(i)).

Interest will cease to accrue on each Bond on the due date for redemption unless, upon due presentation, payment of principal is improperly withheld or refused, in which event interest will continue to accrue (both before and after judgment) at the Interest Rate in the manner provided in this Condition 6 to the Relevant Date (as defined in Condition 6(i)).

In the case of Class C Bonds and Class D Bonds only, if, on any Interest Payment Date, prior to delivery of an enforcement notice under Condition 11, there are insufficient funds available to the Issuer to pay such accrued interest, it 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 Issuer Pre-Enforcement Payments Priorities, sufficient funds available to pay such deferred amounts (including any interest accrued thereon); and (ii) the Interest Payment Date of the last maturing Bond which ranks in priority to the Class C Bonds or the Class D Bonds, as the case may be. Interest will accrue on such deferred interest at the rate otherwise payable on unpaid principal of such Class C Bonds or Class D Bonds, as the case may be.

If any Maximum Interest Rate or Minimum Interest Rate is specified in the relevant Pricing Supplement, then the Interest Rate shall in no event be greater than the maximum or be less than the minimum so specified, as the case may be.

(b) Business Day Convention

If any date referred to in these Conditions or the relevant Pricing Supplement is specified to be subject to adjustment in accordance with a Business Day Convention and would otherwise fall on a day which is not a Business Day, then if the Business Day Convention specified in the relevant Pricing Supplement is:

(i) the Following Business Day Convention, such date shall be postponed to the next day which is a Business Day;

(ii) the Modified Following Business Day Convention, such 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 date shall be brought forward to the immediately preceding Business Day; or

(iii) the Preceding Business Day Convention, such date shall be brought forward to the immediately preceding Business Day.

(c) Floating Rate Bonds

This Condition 6(c) is applicable only if the relevant Pricing Supplement specifies the Bonds as Floating Rate Bonds.

If Screen Rate Determination is specified in the relevant Pricing Supplement as the manner in which the Interest Rate(s) is/are to be determined, the Interest Rate applicable to the Bonds for each Interest Period will be determined by the Agent Bank on the following basis:

(i) if the Page displays a rate which is a composite quotation or customarily supplied by one entity, the Agent Bank will determine the Relevant Rate (as defined in Condition 6(i)) which appears on the Page (as defined in Condition 6(i)) as of the Relevant Time on the relevant Interest Determination Date (as defined in Condition 6(i));

(ii) in any other case, the Agent Bank will determine the arithmetic mean of the Relevant Rates which appear on the Page as of the Relevant Time on the relevant Interest Determination Date;

(iii) if, in the case of (i) above, such rate does not appear on that Page or, in the case of (ii) above, fewer than two such rates appear on that Page or if, in either case, the Page is unavailable, the Agent Bank will:

(1) request the principal Relevant Financial Centre (as defined in Condition 6(i)) office of each of the Reference Banks (as defined in Condition 6(i)) to provide a quotation of the Relevant Rate at approximately the Relevant Time on the relevant Interest Determination Date to prime banks in the Relevant Financial Centre interbank market (or, if appropriate, money market) in an amount that is representative for a single transaction in that market at that time; and

(2) determine the arithmetic mean of such quotations; and

(iv) if fewer than two such quotations are provided as requested, the Agent Bank will determine the arithmetic mean of the rates (being the nearest to the Relevant Rate, as determined by the Agent Bank) quoted by major banks in the Relevant Financial Centre of the Relevant Currency (as defined in Condition 6(i)), selected by the Agent Bank, at approximately 11.00 a.m. (local time in the Relevant Financial Centre of the Relevant Currency) on the first day of the relevant Interest Period (as defined in Condition 6(i)) for loans in the Relevant Currency to leading European banks for a period equal to the relevant Interest Period and in the Representative Amount (as defined in Condition 6(i)),

and the Interest Rate for such Interest Period shall be the sum of the Margin (as defined in Condition 6(i)) and the rate or (as the case may be) the arithmetic mean so determined. However, if the Agent Bank is unable to determine a rate or (as the case may be) an arithmetic mean in accordance with the above provisions in relation to any Interest Period, the Interest Rate applicable to the Bonds during such Interest Period will be the sum of the Margin and the rate (or as the case may be) the arithmetic mean last determined in relation to the Bonds in respect of a preceding Interest Period.

If ISDA Determination is specified in the relevant Pricing Supplement as the manner in which the Interest Rate(s) is/are to be determined, the Interest Rate(s) applicable to the Bonds for each Interest Period will be the sum of the Margin and the relevant ISDA Rate where "**ISDA Rate**" in relation to any

Interest Period means a rate equal to the Floating Rate (as defined in the ISDA Definitions) that would be determined by the Agent Bank under an interest rate swap transaction if the Agent Bank were acting as calculation agent for that interest rate swap transaction under the terms of an agreement incorporating the ISDA Definitions and under which:

(i) the Floating Rate Option (as defined in the ISDA Definitions) is as specified in the relevant Pricing Supplement;

(ii) the Designated Maturity (as defined in the ISDA Definitions) is the Specified Duration (as defined in Condition 6(i)); and

(iii) the relevant Reset Date (as defined in the ISDA Definitions) is either (1) if the relevant Floating Rate Option is based on LIBOR for a currency, the first day of that Interest Period, (2) if the relevant Floating Rate Option is based on EURIBOR, the first day of that Interest Period or (3) in any other case, as specified in the relevant Pricing Supplement.

Notwithstanding any term of these Conditions, for so long as any Class R Bonds are held by, for or on behalf of the Issuer, or any affiliate of the Issuer, such Class R Bonds will not accrue any interest.

(d) Fixed Rate Bonds

This Condition 6(d) is applicable only if the relevant Pricing Supplement specifies the Bonds as Fixed Rate Bonds.

The Interest Rate applicable to the Bonds for each Interest Period will be the fixed rate specified in the relevant Pricing Supplement.

(e) Indexed Bonds

This Condition 6(e) is applicable only if the relevant Pricing Supplement specifies the Bonds as Indexed Bonds.

Payments of principal on, and the interest payable in respect of, the Bonds will be subject to adjustment for indexation and to the extent set out in Condition 7(b). The Interest Rate applicable to the Bonds for each Interest Period will be at the rate specified in the relevant Pricing Supplement.

(f) Rounding

For the purposes of any calculations required pursuant to these Conditions (unless otherwise specified):

(i) all percentages resulting from such calculations will be rounded, if necessary, to the nearest one hundred-thousandth of a percentage point (with halves being rounded up);

(ii) all figures will be rounded to seven significant figures (with halves being rounded up); and

(iii) all currency amounts which fall due and payable will be rounded to the nearest unit of such currency (with halves being rounded up). For these purposes, "**unit**" means, with respect to any currency other than euro, the lowest amount of such currency which is available as legal tender in the country of such currency and, with respect to euro, means 0.01 euro.

(g) Calculations

The amount of interest payable in respect of any Bond for each Interest Period shall be calculated by multiplying the product of the Interest Rate and the Principal Amount Outstanding of such Bond during that Interest Period by the Day Count Fraction (as defined in Condition 6(i)), unless an Interest Amount is specified in respect of such period in the relevant Pricing Supplement, in which case the amount of interest payable in respect of such Bond for such Interest Period will equal such Interest Amount.

(h) Determination and Publication of Interest Rates, Interest Amounts, Redemption Amounts and Instalment Amounts

As soon as practicable after the Relevant Time on each Interest Determination Date or such other time on such date as the Agent Bank may be required to calculate any Redemption Amount or Instalment Amount, obtain any quote or make any determination or calculation, the Agent Bank will determine the Interest Rate and calculate the amount of interest payable (the "**Interest Amounts**") in respect of each Authorised Denomination of Bonds for the relevant Interest Period, calculate the Redemption Amount or Instalment Amount, obtain such quote or make such determination or calculation, as the case may be, and cause the Interest Rate and the Interest Amounts for each Interest

Period and the relevant Interest Payment Date and, if required to be calculated, the Redemption Amount or any Instalment Amount to be notified, in the case of Bearer Bonds, to the Paying Agents or, in the case of Registered Bonds, the Transfer Agents and the Registrar, the Bond Trustee, the Issuer, the Bondholders and the Luxembourg Stock Exchange as soon as possible after its determination but in no event later than (i) (in case of notification to the Luxembourg Stock Exchange) the commencement of the relevant Interest Period, if determined prior to such time, in the case of an Interest Rate and Interest Amount, or (ii) in all other cases, the fourth Business Day after such determination. The Interest Amounts and the Interest Payment Date so published may subsequently be amended (or appropriate alternative arrangements made by way of adjustment) without notice in the event of an extension or shortening of the Interest Period. If the Bonds become due and payable under Condition 11, the accrued interest and the Interest Rate payable in respect of the Bonds shall nevertheless continue to be calculated as previously provided in accordance with this Condition but no publication of the Interest Rate or the Interest Amount so calculated need be made unless otherwise required by the Bond Trustee. The determination of each Interest Rate, Interest Amount, Redemption Amount and Instalment Amount, the obtaining of each quote and the making of each determination or calculation by the Agent Bank or, as the case may be, the Bond Trustee pursuant to this Condition 6 or Condition 7, shall (in the absence of manifest error) be final and binding upon all parties.

(i) Definitions

In these Conditions, unless the context otherwise requires, the following defined terms shall have the meanings set out below.

"**Business Day**" means:

(i) 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 Business Centre specified in the relevant Pricing Supplement; and

(ii) 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 Relevant Currency (which in the case of a payment in US Dollars shall be New York) and in each (if any) Additional Business Centre specified in the relevant Pricing Supplement.

"**Day Count Fraction**" means, in respect of the calculation of an amount of interest on any Bond for any period of time (whether or not constituting an Interest Period, the "**Calculation Period**"):

(i) if "**Actual/Actual (ISMA)**" is specified, the sum of, for each Determination Period (as specified in the Pricing Supplement) contained either wholly or in part in the Calculation Period, the number of days in the Determination Period falling in the Calculation Period divided by the product of (x) the number of days in the Determination Period and (y) the number of Determination Dates (as specified in the Pricing Supplement) that would occur in one calendar year;

(ii) if "**Actual/365**" or "**Actual/Actual**" is specified, the actual number of days in the Calculation Period divided by 365 (or, if any portion of that Calculation Period falls in a leap year, the sum of (1) the actual number of days in that portion of the Calculation Period falling in a leap year divided by 366, and (2) the actual number of days in that portion of the Calculation Period falling in a non-leap year divided by 365);

(iii) if "**Actual/365 (Fixed)**" is specified, the actual number of days in the Calculation Period divided by 365;

(iv) if "**Actual/360**" is specified, the actual number of days in the Calculation Period divided by 360;

(v) if "**30/360**", "**360/360**" or "**Bond Basis**" is specified, the number of days in the Calculation 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 (1) the last day of the Calculation Period is the 31st day of a month but the first day of the Calculation Period is a day other than the 30th or 31st 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 (2) the last day of the Calculation 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

(vi) if "**30E/360**" or "**Eurobond Basis**" is specified, the number of days in the Calculation 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 Calculation Period) unless, in the case of the final Calculation Period, the last day of such 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;

"**euro**" means the lawful currency of the Participating Member States;

"**Interest Commencement Date**" means the Issue Date or such other date as may be specified in the relevant Pricing Supplement;

"**Interest Determination Date**" means, with respect to an Interest Rate and an Interest Period, the date specified as such in the relevant Pricing Supplement or, if none is so specified, the day falling two Business Days in London prior to the first day of such Interest Period (or if the specified currency is sterling the first day of such Interest Period);

"**Interest Payment Date**" means the date(s) specified as such in the relevant Pricing Supplement;

"**Interest Period**" means the period beginning on (and including) the Interest Commencement Date and ending on (but excluding) the first Interest Payment Date and each successive period beginning on (and including) an Interest Payment Date and ending on (but excluding) the next succeeding Interest Payment Date;

"**Interest Rate**" means the rate of interest payable from time to time in respect of the Bonds and which is either specified in, or calculated in accordance with the provisions of, these Conditions and/or the relevant Pricing Supplement;

"**ISDA Definitions**" means the 2000 ISDA Definitions (as amended and updated as at the date of issue of the first Bonds of the relevant Sub-Class as published by the International Swaps and Derivatives Association, Inc. (formerly the International Swap Dealers Association, Inc.)).

"**Issue Date**" means the date specified in the relevant Pricing Supplement;

"**Margin**" means the rate per annum (expressed as a percentage) specified in the relevant Pricing Supplement;

"**Page**" means such page, section, caption, column or other part of a particular information service (including the Reuter Monitor Money Rates Service ("**Reuters**") and the Dow Jones Telerate Service ("**Telerate**")) as may be specified in the relevant Pricing Supplement, or such other page, section, caption, column or other part as may replace the same on that information service or on such other information service, in each case as may be nominated by the person or organisation providing or sponsoring the information appearing there for the purpose of displaying comparable rates or prices;

"**Participating Member State**" means a Member State of the European Community which adopts the euro as its lawful currency in accordance with the Treaty establishing the European Community (as amended by the Treaty on European Union and the Treaty of Amsterdam), and "**Participating Member States**" means all of them;

"**Principal Amount Outstanding**" means, in relation to a Bond, Sub-Class or Class, the original face value thereof less any repayment of principal made to the Holder(s) thereof in respect of such Bond, Sub-Class or Class;

"**Redemption Amount**" means the amount provided under Condition 8(b), unless otherwise specified in the relevant Pricing Supplement;

"**Reference Banks**" means the institutions specified as such or, if none, four major banks selected by the Agent Bank in the interbank market (or, if appropriate, money market) which is most closely connected with the Relevant Rate as determined by the Agent Bank, on behalf of the Issuer, in its sole and absolute discretion;

"**Relevant Currency**" means the currency specified as such in the relevant Pricing Supplement or, if none is specified, the currency in which the Bonds are denominated;

"**Relevant Date**" means the earlier of (a) the date on which all amounts in respect of the Bonds have been paid, and (b) five days after the date on which all of the Principal Amount Outstanding has been received by the Principal Paying Agent or the Registrar, as the case may be, and notice to that effect has been given to the Bondholders in accordance with Condition 17;

"**Relevant Financial Centre**" means, with respect to any Bond, the financial centre specified as such in the relevant Pricing Supplement or, if none is so specified, the financial centre with which the Relevant Rate is most closely connected as determined by the Agent Bank;

"**Relevant Rate**" means the offered rate for a Representative Amount of the Relevant Currency for a period (if applicable) equal to the Specified Duration (or such other rate as shall be specified in the relevant Pricing Supplement);

"**Relevant Time**" means, with respect to any Interest Determination Date, the local time in the Relevant Financial Centre specified in the relevant Pricing Supplement or, if none is specified, the local time in the Relevant Financial Centre at which it is customary to determine bid and offered rates in respect of deposits in the Relevant Currency in the interbank market or, if appropriate, money market in the Relevant Financial Centre;

"**Representative Amount**" means, with respect to any rate to be determined on an Interest Determination Date, the amount specified in the relevant Pricing Supplement as such or, if none is specified, an amount that is representative for a single transaction in the relevant market at the time;

"**Specified Duration**" means, with respect to any Floating Rate (as defined in the ISDA Definitions) to be determined on an Interest Determination Date, the Designated Maturity specified in the relevant Pricing Supplement or, if none is specified, a period of time equal to the relative Interest Period;

"**TARGET Settlement Day**" means any day on which the TARGET system is open; and

"**TARGET system**" means the Trans-European Automated Real-Time Gross Settlement Express Transfer system.

(j) Agent Bank and Reference Banks

The Issuer will procure that there shall at all times be an Agent Bank and four Reference Banks selected by the Issuer acting through the Agent Bank with offices in the Relevant Financial Centre if provision is made for them in these Conditions applicable to this Bond and for so long as it is outstanding. If any Reference Bank (acting through its relevant office) is unable or unwilling to continue to act as a Reference Bank, then the Issuer acting through the Agent Bank will select another Reference Bank with an office in the Relevant Financial Centre to act as such in its place. If the Agent Bank is unable or unwilling to act as such or if the Agent Bank fails duly to establish the Interest Rate for any Interest Period or to calculate the Interest Amounts or any other requirements, the Issuer will appoint (with the prior written consent of the Bond Trustee) a successor to act as such in its place. The Agent Bank may not resign its duties without a successor having been appointed as aforesaid.

(k) Determination or Calculation by Bond Trustee

If the Agent Bank does not at any time for any reason determine any Interest Rate, Interest Amount, Redemption Amount, Instalment Amount or any other amount to be determined or calculated by it, the Bond Trustee, shall determine such Interest Rate, Interest Amount, Redemption Amount, Instalment Amount or other amount as aforesaid at such rate or in such amount as in its absolute discretion (having regard as it shall think fit to the procedures described above, but subject to the terms of the Trust Deed) it shall deem fair and reasonable in all the circumstances or, subject as aforesaid, apply the foregoing provisions of this Condition, with any consequential amendments, to the extent that, in its sole opinion, it can do so and in all other respects it shall do so in such manner as it shall, in its absolute discretion, deem fair and reasonable in the circumstances, and each such determination or calculation shall be deemed to have been made by the Agent Bank.

7. Indexation

This Condition 7 is applicable only if the relevant Pricing Supplement specifies the Bonds as Indexed Bonds including Limited Indexed Bonds (as defined below).

(a) Definitions

"**Base Index Figure**" means (subject to Condition 7(c)(i)) 171.7.

"**Index**" or "**Index Figure**" means, subject as provided in Condition 7(c)(i), the UK Retail Price Index (RPI) (for all items) published by the Central Statistical Office (January 1987 = 100) or any comparable index which may replace the UK Retail Price 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 Condition 7(c) and (e), 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.

''**Limited Index Ratio**'' means (a) in respect of any month prior to the relevant Issue Date, the Index Ratio for that month; (b) in respect of any Limited Indexation Month after the relevant Issue Date, the product of the Limited Indexation Factor for that month and the Limited Index Ratio as previously calculated in respect of the month twelve months prior thereto; and (c) in respect of any other month, the Limited Index Ratio as previously calculated in respect of the most recent Limited Indexation Month.

''**Limited Indexation Factor**'' means, in respect of a Limited Indexation Month, the ratio of the Index Figure applicable to that month divided by the Index Figure applicable to the month twelve months prior thereto, provided that (a) if such ratio is greater than the Maximum Indexation Factor specified in the relevant Pricing Supplement, it shall be deemed to be equal to such Maximum Indexation Factor and (b) if such ratio is less than the Minimum Indexation Factor specified in the relevant Pricing Supplement, it shall be deemed to be equal to such Minimum Indexation Factor.

''**Limited Indexation Month**'' means any month specified in the relevant Pricing Supplement for which a Limited Indexation Factor is to be calculated.

''**Limited Indexed Bonds**'' means Indexed Bonds to which a Maximum Indexation Factor and/or a Minimum Indexation Factor (as specified in the relevant Pricing Supplement) applies.

''**Reference Gilt**'' means the Treasury Stock specified in the relevant Pricing Supplement for so long as such stock is in issue, and thereafter such issue of index-linked Treasury Stock determined to be appropriate by a gilt-edged market maker or other adviser selected by the Issuer and approved by the Bond Trustee (an ''**Indexation Adviser**'').

(b) Application of the appropriate 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, or Limited Index Ratio in the case of Limited Indexed Bonds, 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) *Change in base:* If at any time and from time to time the Index is changed by the substitution of a new base therefor, then with effect from the calendar month from and including which such substitution takes effect (1) the definition of ''**Index**'' and ''**Index Figure**'' in Condition 7(a) shall be deemed to refer to the new date or month in substitution for January 1987 (or, as the case may be, to such other date or month as may have been substituted therefor), and (2) the new Base Index Figure shall be the product of the existing Base Index Figure (being at the Initial Issue Date 171.7) and the Index Figure immediately following such substitution, divided by the Index Figure immediately prior to such substitution.

(ii) *Delay in publication of Index:* If the Index Figure which is normally published in the seventh month and which relates 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 on which such payment is due (the ''**date for payment**''), the Index Figure applicable to the month in which the date for payment falls shall be (1) such substitute index figure (if any) as the Bond Trustee, considers 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 an Indexation Advisor and approved by the Bond Trustee, or (2) if no such determination is made by such Indexation Adviser within 7 days, the Index Figure last published (or, if later, the substitute index figure last determined pursuant to Condition 7(c)(i)) before the date for payment.

(d) Application of Changes

Where the provisions of Condition 7(c)(ii) 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 Condition 7(c)(ii)(2), the Index Figure relating to the relevant month is subsequently published while a Bond is still outstanding, then:

(i) in relation to a payment of principal or interest in respect of such Bond other than upon final redemption 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 Condition 7(c)(ii)(2), 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; and

(ii) in relation to a payment of principal or interest upon final redemption, no subsequent adjustment to amounts paid will be made.

(e) Cessation of or Fundamental Changes to the Index

(i) If (1) the Bond Trustee has been notified by the Agent Bank that the Index has ceased to be published or (2) 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 an 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.

(ii) If the Issuer and the Bond Trustee fail to reach agreement as mentioned above within 20 business days following the giving of notice as mentioned in paragraph (i), a bank or other person in London shall be appointed by the Issuer and the Bond Trustee or, failing agreement on and the making of 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 and of any Indexation Adviser and of any of the Issuer and the Bond Trustee in connection with such appointment shall be borne by the Issuer.

(iii) 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 and the Issuer agree are appropriate to give effect to such adjustment or replacement. Such amendments shall be effective from the date of such notification and binding upon the Bond Trustee, the Financial Guarantors, the other Issuer Secured Creditors, the Issuer and the Bondholders, and the Issuer shall give notice to the Bondholders in accordance with Condition 17 of such amendments as promptly as practicable following such notification.

8. Redemption, Purchase and Cancellation

(a) Partial and Final Redemption

Unless previously redeemed, or purchased and cancelled as provided below, or unless such Bond is stated in the relevant Pricing Supplement as having no fixed maturity date, each Bond will be redeemed at its Principal Amount Outstanding (in the case of Indexed Bonds, as adjusted in accordance with Condition 7(b)), on the date or dates (or, in the case of Floating Rate Bonds, on the Interest Payment Date(s) upon which interest is payable) specified in the relevant Pricing Supplement.

(b) Optional Redemption

Subject as provided below, upon giving not more than 60 nor less than 30 days' notice to the Bond Trustee, the Issuer Security Trustee, the Issuer Instructing Group and the Bondholders, the Issuer may (prior to the Maturity Date) redeem any Sub-Class of the Bonds in whole or in part (but on a pro rata basis only) on any Interest Payment Date at their Redemption Amount, provided that Floating Rate Bonds may not be redeemed before the date specified in the relevant Pricing Supplement, as follows:

(i) In respect of Fixed Rate Bonds, the Redemption Amount will be an amount equal to the higher of (i) their Principal Amount Outstanding 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 such 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 Benchmark Gilt (as defined below) while that stock is in issue, and thereafter such UK 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, plus accrued but unpaid interest on the Principal Amount Outstanding.

For the purposes of this Condition 8(b)(i), "**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" published 8 June 1998 with effect from 1 November 1998, page 4; "**Reference Date**" means the date which is two Business Days prior to the despatch of the notice of redemption under this Condition 8(b)(i); and "**Benchmark Gilt**" means the Treasury Stock specified in the relevant Pricing Supplement.

(ii) In respect of Floating Rate Bonds, the Redemption Amount will be the Principal Amount Outstanding plus any premium for early redemption in certain years (as specified in the relevant Pricing Supplement) plus any accrued but unpaid interest on the Principal Amount Outstanding.

(iii) In respect of Indexed Bonds, the Redemption Amount will be the higher of (i) the Principal Amount Outstanding (as adjusted in accordance with Condition 7(b)) and (ii) the price determined to be appropriate (without any additional indexation beyond the implicit indexation in such determined price) by a financial adviser in London (selected by the Issuer and approved by the Bond Trustee) as being the price at which the Gross Real Redemption Yield (as defined below) on the Bonds on the Reference Date (as defined below) is equal to the Gross Real Redemption Yield at 3:00 p.m. (London time) on the Reference Date on the Reference Gilt while that stock is in issue, and thereafter such UK 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, plus accrued but unpaid interest (as adjusted in accordance with Condition 7(b)) on the Principal Amount Outstanding.

For the purposes of this Condition 8(b)(iii), "**Gross Real 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" published 8 June 1998 with effect from 1 November 1998, page 5; "**Reference Date**" means the date which is two Business Days prior to the despatch of the notice of redemption under this Condition 8(b)(iii).

In any such case, prior to giving any such notice, the Issuer must certify (as further specified in the Issuer Transaction Documents) to the Bond Trustee that it will have the funds, not subject to any interest of any other person, required to redeem the Bonds as aforesaid.

The Issuer may not, without the prior written consent of the Issuer Security Trustee (acting on instructions of the Issuer Instructing Group), redeem any Class C Bonds before (i) the periodic review to be undertaken by the Director General of Water Services in March 2005 or (ii) if that review is appealed, 1 October 2005.

(c) Redemption for Index Event, Taxation and Other Reasons

Redemption for Index Events: Upon the occurrence of any Index Event (as defined below), the Issuer may, upon giving not more than 60 nor less than 30 days' notice to the Bond Trustee, the Issuer Security Trustee, the Issuer Instructing Group and the holders of the Indexed Bonds in accordance with Condition 17, redeem all (but not some only) of the Indexed Bonds of all Sub-Classes on any Interest Payment Date at the Principal Amount Outstanding plus accrued but unpaid interest and any amounts in respect of indexation on such Indexed Bonds. No single Sub-Class of Indexed Bonds may be redeemed in these circumstances unless all the other Sub-Classes of Indexed Bonds are also redeemed at the same time. Before giving any such notice, the Issuer shall provide to the Bond Trustee the Issuer Security Trustee, and the Issuer Instructing Group a certificate signed by an authorised signatory (a) 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 and (b) confirming that the Issuer will have sufficient funds on such Interest Payment Date to effect such redemption.

"**Index Event**" means (i) if the Index Figure for three consecutive months falls to be determined on the basis of an Index Figure previously published as provided in Condition 7(c)(ii) and the Bond Trustee has been notified by the Agent Bank 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 the holders of the Reference Gilt, and (in either case) no amendment or substitution of the Index has been advised by the Indexation Advisor to the Issuer and such circumstances are continuing.

Redemption for Taxation 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 the Cayman Islands 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 under the Intercompany Loan Agreements upon satisfying the conditions for substitution of the Issuer as set out in the Issuer STID (and referred to in Condition 15(c)). 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, upon giving not more than 60 nor less than 30 days' notice to the Bond Trustee, the Issuer Security Trustee, the Issuer Instructing Group and the Bondholders in accordance with Condition 17, redeem all (but not some only) of the Bonds of all Sub-Classes on any Interest Payment Date at their Principal Amount Outstanding plus accrued but unpaid interest thereon and, in the case of Indexed Bonds, amounts in respect of indexation. Before giving any such notice, the Issuer shall provide to the Bond Trustee, the Issuer Security Trustee and the Issuer Instructing Group a certificate signed by an authorised signatory (a) 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 and (b) confirming that the Issuer will have sufficient funds on such Interest Payment Date to discharge all its liabilities in respect of the Bonds and any amounts to be paid in priority to, or *pari passu* with, the Bonds under the Issuer Pre-Enforcement Payments Priorities.

Redemption on Prepayment of Intercompany Loan Agreement: If DCC gives notice to the Issuer under an Intercompany Loan Agreement that it intends to prepay all or part of any advance made under such Intercompany Loan Agreement and such advance was funded by the Issuer from the proceeds of the issue of a Sub-Class of Bonds, the Issuer shall, upon giving not more than 60 nor less than 30 days' notice to the Bond Trustee, the Issuer Security Trustee, the Issuer Instructing Group and the Bondholders in accordance with Condition 17, (where such advance is being prepaid in whole) redeem all of the Bonds of that Sub-Class or (where part only of such advance is being prepaid) the proportion of the relevant Sub-Class of Bonds which the proposed prepayment amount bears to the amount of the relevant advance. In the case of a voluntary prepayment, the relevant Bonds will be redeemed at their Redemption Amount plus accrued but unpaid interest and, in the case of any other prepayment, the relevant Bonds will be redeemed at their Principal Amount Outstanding plus accrued but unpaid interest.

(d) Purchase of Bonds other than R Bonds

The Issuer may, provided that no Issuer Event of Default has occurred and is continuing, purchase Bonds other than Class R Bonds (or any of them) (provided that all unmatured Receipts and Coupons and unexchanged Talons (if any) appertaining thereto are attached or surrendered therewith) in the open market or otherwise at any price. Any purchase by tender shall be made available to all Bondholders alike.

If not all the Bonds which are in registered form are to be purchased, upon surrender of the existing Registered Bond Certificate, the Registrar shall forthwith upon the written request of the Bondholder concerned issue a new Registered Bond Certificate in respect of the Bonds which are not to be purchased and despatch such Registered Bond Certificate to the Bondholder (at the risk of the Bondholder and to such address as the Bondholder may specify in such request).

Whilst the Bonds are represented by a Global Bond or Regulation S Global Bond Certificate (a "Global Bond Certificate"), the relevant Global Bond or Global Bond Certificate will be endorsed to reflect the Principal Amount Outstanding of Bonds to be so redeemed or purchased.

(e) Purchase of Class R Bonds

(i) The Issuer may purchase Class R Bonds on any day in the open market at any price which does not exceed their Principal Amount Outstanding plus accrued interest and in relation to such purchase shall, for so long as the Class R Bonds are admitted to trading on the Luxembourg Stock Exchange, comply with all applicable regulations of the Luxembourg Stock Exchange and may, at its option, hold, resell or cancel any such Class R Bonds held by it from time to time, provided that the Issuer shall not be entitled to resell such Class R Bonds:

(a) if any Issuer Event of Default exists;

(b) (in the case of any Class R Extension Amount (as defined in Condition 8(e)(vii)) if any DCC Event of Default (as defined under the Master Framework Agreement) exists; or

(c) at any time after 31 March 2006.

(ii) The Issuer will (save to the extent that Condition 8(e)(iii) applies and save where an Issuer Event of Default exists) on any Interest Payment Date falling on or prior to 31 March 2006 repurchase all Class R Bonds outstanding on each Interest Payment Date at a price which is equal to their Principal Amount Outstanding, plus accrued but unpaid interest thereon. The Issuer may at its option cancel, hold or resell all or any of the Class R Bonds so purchased, provided that the Issuer shall not be entitled to resell any such Class R Bonds:

(a) if any Issuer Event of Default exists;

(b) (in the case of any Class R Extension Amount) if any DCC Event of Default exists; or

(c) at any time after the 31 March 2006.

(iii) Notwithstanding the provisions of Condition 8(e)(ii), the Issuer shall not, during the Underwriting Period, be obliged to repurchase any Class R Bonds in respect of which it holds insufficient funds to effect such repurchase in accordance with Condition 8(e)(ii), if such insufficiency arises as a result of any Class R Underwriter failing to agree under the Class R Underwriting Agreement to purchase Class R Bonds from the Issuer. The Class R Bonds to be repurchased on an Interest Payment Date, in respect of which there are insufficient funds to effect such repurchase in full, shall be repurchased pro rata from the holders of the Class R Bonds. Any Class R Bonds not so repurchased shall remain outstanding and the provisions of sub-paragraphs (a) and (b) of Condition 8(e)(ii) shall not apply to such Class R Bonds until such time as they are subsequently repurchased by the Issuer.

(iv) If, by virtue of the operation of either of Condition 8(e)(ii) or 8(e)(iii), the Issuer is not obliged to repurchase the Class R Bonds on any Interest Payment Date, the Issuer shall, immediately upon becoming aware that it will not be repurchasing such Class R Bonds by virtue of the operation of either of Condition 8(e)(ii) or 8(e)(iii) (and in any event, by no later than 11.00 a.m. on the Interest Payment Date upon which it would otherwise have repurchased such Class R Bonds), give notice to the Class R Bondholders, the Rating Agencies and the Principal Paying Agent (in the case of Bearer Bonds) and the Transfer

Agents and the Registrar (in the case of Registered Bonds), in accordance with the provisions of Condition 17, specifying the amount of Class R Bonds which will not be repurchased on such Interest Payment Date.

(v) Notwithstanding the provisions of Conditions 8(e)(i) and 8(e)(ii), the Issuer shall not be entitled to resell any Class R Bonds which it has repurchased following the occurrence of any of the events referred to in sub-paragraphs (a), (b) or (c) of either of Conditions 8(e)(i) and 8(e)(ii). Further, while any Issuer Event of Default exists, Class R Bonds may not be repurchased and shall only be redeemed in accordance with Conditions 8(b) and (c). Any Class R Bonds so redeemed shall be cancelled upon redemption. The Class R Bonds (if any) which are the first Class R Bonds to be resold by the Issuer following the occurrence of any of the events referred to in sub-paragraphs (b) or (c) of either of Conditions 8(e)(i) and 8(e)(ii) shall be deemed to be, and shall for all purposes be treated as, Class R Extension Amounts of the relevant Class.

(vi) Any Class R Bonds held by or on behalf of the Issuer on the close of business on 31 March 2006 shall be cancelled and any Class R Bonds purchased by the Issuer on or after such Interest Payment Date shall be cancelled immediately upon such repurchase.

(vii) In these Conditions:

"**affiliate**" means in relation to any person, any entity controlled, directly or indirectly, by that person, any entity that controls directly or indirectly, that person or any entity, directly or indirectly under common control with that person and, for this purpose, "control" means control as defined in the Companies Act 1985;

"Class R Extension Amount" means the amount (if any) by which, on any Class R Further Drawing Date, the face value of the Class R Bonds being resold by the Issuer on such day exceeds the Principal Amount Outstanding of the Class R Bonds held by persons, other than the Issuer or any affiliate of the Issuer, on the day which immediately preceded such Class R Further Drawing Date;

"**Class R Further Drawing Date**" means any date upon which Class R Bonds are resold;

"**Class R Underwriters**" means each of the parties described as such in the Class R Underwriting Agreement and its successors and assigns; and

"**Underwriting Period**" means the period from the date of the Class R Underwriting Agreement up to and including 31 March 2006.

(f) Redemption by Instalments

Unless previously redeemed, purchased and cancelled as provided in this Condition 8, each Bond which provides for Instalment Dates (as specified in the relevant Pricing Supplement) and Instalment Amounts (as specified in the relevant Pricing Supplement) will be partially redeemed on each Instalment Date at the Instalment Amount.

(g) Cancellation

In respect of all Bonds purchased by or on behalf of the Issuer other than as provided in Condition 8(e), the Bearer Bonds or the Registered Bond Certificates shall be surrendered to or to the order of the Principal Paying Agent or the Registrar, as the case may be, for cancellation and, if so surrendered, will, together with all Bonds redeemed by the Issuer, be cancelled forthwith (together with, in the case of Bearer Bonds, all unmatured Receipts and Coupons and unexchanged Talons attached thereto or surrendered therewith). Any Bonds so surrendered for cancellation may not be reissued or resold and the obligations of the Issuer in respect of any such Bonds shall be discharged.

9. Payments

(a) Bearer Bonds

Payments to the Bondholders of principal (or, as the case may be, Redemption Amounts or other amounts payable on redemption) and interest (or, as the case may be, Interest Amounts) in respect of Bearer Bonds will, subject as mentioned below, be made against presentation and surrender of the relevant Receipts (in the case of payment of Instalment Amounts other than on the due date for final redemption and provided that the Receipt is presented for payment together with its relative Bond), Bonds (in the case of all other payments of principal and, in the case of interest, as specified in Condition 9(f)) or Coupons (in the case of interest, save as specified in Condition 9(f)), as the case may

be, at the specified office of any Paying Agent outside the United States of America by transfer to an account denominated in the currency in which such payment is due with, or (in the case of Definitive Bonds only) a cheque payable in that currency drawn on, a bank in (i) the principal financial centre of that currency provided that such currency is not euro, or (ii) the principal financial centre of any Participating Member State if that currency is euro.

(b) *Registered Bonds*

Payments of principal (or, as the case may be, Redemption Amounts) in respect of Registered Bonds will be made to the holder (or the first named of joint holders) of such Bond against presentation and surrender of the relevant Registered Bond Certificate at the specified office of the Registrar and in the manner provided in Condition 9(a).

Payments of instalments in respect of Registered Bonds will be made to the holder (or the first named of joint holders) of such Bond against presentation of the relevant Registered Bond Certificate at the specified office of the Registrar in the manner provided in Condition 9(a) above and annotation of such payment on the Register and the relevant Registered Bond Certificate.

Interest (or, as the case may be, Interest Amounts) on Registered Bonds payable on any Interest Payment Date will be paid to the holder (or the first named if joint holders) on the fifteenth day before the due date for payment thereof (the "**Record Date**"). Payment of interest or Interest Amounts on each Registered Bond will be made in the currency in which such payment is due by cheque drawn on a bank in (a) the principal financial centre of the country of the currency concerned, provided that such currency is not euro, or (b) the principal financial centre of any Participating Member State if that currency is euro and mailed to the holder (or to the first named of joint holders) of such Bond at its address appearing in the Register. Upon application by the Bondholder to the specified office of the Registrar before the relevant Record Date, such payment of interest may be made by transfer to an account in the relevant currency maintained by the payee with a bank in (a) the principal financial centre of the country of that currency provided that such currency is not euro, or (b) the principal financial centre of any Participating Member State if that currency is euro.

(c) *Payments in the United States of America*

Notwithstanding the foregoing, if any Bearer Bonds are denominated in U.S. dollars, payments in respect thereof may be made at the specified office of any Paying Agent in New York City in the same manner as aforesaid if:

(i) the Issuer shall have appointed Paying Agents with specified offices outside the United States of America with the reasonable expectation that such Paying Agents would be able to make payment of the amounts on the Bonds in the manner provided above when due;

(ii) payment in full of such amounts at all such offices is illegal or effectively precluded by exchange controls or other similar restrictions on payment or receipt of such amounts; and

(iii) such payment is then permitted by the law of the United States of America, without involving, in the opinion of the Issuer, adverse tax consequences to the Issuer.

(d) *Payments subject to fiscal laws; payments on Global Bonds and Registered Bonds*

All payments are subject in all cases to any applicable fiscal or other laws, regulations and directives, but without prejudice to the provisions of this Condition 9. No commission or expenses shall be charged to the Bondholders, Couponholders or Receiptholders (if any) in respect of such payments.

Payments of principal (or Redemption Amounts) and interest (or Interest Amounts) in respect of the Bearer Bonds when represented by a Global Bond or Global Bond Certificate will be made against presentation and surrender or, as the case may be, presentation of the Global Bond or Global Bond Certificate at the specified office of the Principal Paying Agent or the Registrar, as the case may be, subject in all cases to any fiscal or other laws, regulations and directives applicable in the place of payment to the Issuer, the Principal Paying Agent, the Registrar or the holder. A record of each payment so made will be endorsed on the schedule to the Global Bond or the Global Bond Certificate by or on behalf of the Principal Paying Agent or Registrar, as the case may be, which endorsement shall be *prima facie* evidence that such payment has been made.

The holder of a Global Bond or Global Bond Certificate shall be the only person entitled to receive payments of principal (or Redemption Amounts) and interest (or Interest Amounts) on the Global Bond or Global Bond Certificate (as the case may be) and the Issuer will be discharged by payment to, or to the order of, the holder of such Global Bond or Global Bond Certificate in respect of each amount paid.

(e) Appointment of the Agents

The Paying Agents, the Agent Bank, the Transfer Agents and the Registrar (the "**Agents**") appointed by the Issuer (and their respective specified offices are listed in the Paying Agency Agreement) or as otherwise appointed pursuant to the Paying Agency Agreement are specified in the relevant Pricing Supplement. The Agents act solely as agents of the Issuer and do not assume any obligation or relationship of agency or trust for or with any holder. The Issuer reserves the right, with the prior written consent of the Bond Trustee, at any time to vary or terminate the appointment of any Agent, and to appoint additional or other Agents, provided that the Issuer will at all times maintain a Principal Paying Agent, a Paying Agent in Luxembourg (so long as any Bonds remain listed on the Luxembourg Stock Exchange) and (while any Registered Bonds remain outstanding) a Transfer Agent in Luxembourg (so long as any Bonds remain listed on the Luxembourg Stock Exchange) and a Registrar, each having a specified office in a European city which, if the Bonds are admitted to listing on a listing authority, stock exchange and/or quotation system and such listing authority, stock exchange and/or quotation system require the appointment of a Paying Agent in a particular place, shall be such place.

(f) Unmatured Coupons and Receipts and unexchanged Talons

(i) Subject to the provisions of the relevant Pricing Supplement, upon the due date for redemption of any Bond which is a Bearer Bond, unmatured Coupons and Receipts relating to such Bond (whether or not attached) shall become void and no payment shall be made in respect of them.

(ii) Upon the date for redemption of any Bond, any unmatured Talon relating to such Bond (whether or not attached) shall become void and no Coupon shall be delivered in respect of such Talon.

(iii) Upon the due date for redemption of any Bond which is redeemable in instalments, all Receipts relating to such Bond having an Instalment Date falling on or after such due date (whether or not attached) shall become void and no payment shall be made in respect of them.

(iv) Where any Bond, which is a Bearer Bond, is presented for redemption without all unmatured Coupons and any unexchanged Talon relating to it, and where any Bearer Bond is presented for redemption without any unexchanged Talon relating to it, redemption shall be made only against the provision of such indemnity as the Issuer may require.

(v) If the due date for redemption of any Bond is not a due date for payment of interest or an Interest Amount, interest accrued from the preceding due date for payment of interest or the Interest Commencement Date, as the case may be, or the Interest Amount payable on such date for redemption shall only be payable against presentation (and surrender if appropriate) of the relevant Bond and Coupon.

(g) Non-Business Days

Subject as provided in the relevant Pricing Supplement, if any date for payment in respect of any Bond, Receipt or Coupon is not a business day, the holder shall not be entitled to payment until the next following business day nor to any interest or other sum in respect of such postponed payment. In this paragraph, "**business day**" means a day (other than a Saturday or a Sunday) on which banks are open for presentation and payment of debt securities and for dealings in foreign currency in London and in the relevant place of presentation and in the other cities referred to in the definition of Business Days and (in the case of a payment in a currency other than euro), where payment is to be made by transfer to an account maintained with a bank in the relevant currency, on which dealings may be carried on in the relevant currency in the principal financial centre of the country of such currency.

(h) Talons

On or after the Interest Payment Date for the final Coupon forming part of a coupon sheet issued in respect of any Bond, the Talon forming part of such coupon sheet may be surrendered at the specified office of any Paying Agent in exchange for a further coupon sheet (and if necessary another Talon for a further coupon sheet) (but excluding any Coupons which may have become void pursuant to Condition 13).

10. Taxation

All payments in respect of the Bonds, Receipts or Coupons will be made (whether by the Issuer, any Paying Agent, the Registrar, the Bond Trustee, the Issuer Security Trustee or the relevant Financial Guarantor, in respect of Class A Bonds) without withholding or deduction for, or on account of, any present or future taxes, duties or charges of whatsoever nature unless the Issuer, any Paying Agent or the Registrar or, where applicable, the Bond Trustee, the Issuer Security Trustee or the relevant Financial Guarantor is required by applicable law to make any payment in respect of the Bonds, Receipts or Coupons subject to any withholding or deduction for, or on account of, any present or future taxes, duties or charges of whatsoever nature. In that event, the Issuer, such Paying Agent, the Registrar, the Bond Trustee, the Issuer Security Trustee or the relevant Financial Guarantor, as the case may be, 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, any Paying Agent, the Registrar, the Bond Trustee, the Issuer 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. The Issuer, any Paying Agent, the Registrar, the Bond 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.

11. Events of Default and Enforcement

(a) Issuer Events of Default

If an Issuer Event of Default (as defined below) occurs and is continuing, then, subject always to the terms of the Issuer STID, the Bond Trustee may at any time and shall (subject, in the case of any of the events referred to in paragraph (ii) below, to the Bond Trustee (in accordance with the provisions of the Trust Deed and the Issuer STID) having certified in writing that in its opinion the happening of such event is materially prejudicial to the Bondholders), upon the Bond Trustee being (i) so requested in writing by holders of at least one quarter in Principal Amount Outstanding of the Most Senior Class of Bonds (as defined below) then outstanding or if so directed by an Extraordinary Resolution (as defined below) of the Most Senior Class of Bonds then outstanding; and (ii) indemnified and/or secured to its satisfaction, subject to the directions of the Issuer Instructing Group, give notice to the Issuer and the Issuer Security Trustee that the Bonds of all Sub-Classes of every Class and Series are, and they shall immediately become, due and repayable, at their respective Redemption Amounts.

Each of the following will constitute an "**Issuer Event of Default**" under the Bonds:

(i) if default is made in the payment of any sum due in respect of the Bonds (or any Sub-Class of them); or

(ii) if the Issuer fails to perform or observe any of its obligations (other than payment obligations referred to in (i) above) under the Bonds (including these Conditions) and, if the Bond Trustee considers that such default can be remedied, such failure continues for a period of 30 days (or such longer period as the Bond Trustee may permit) following the service by the Bond Trustee on the Issuer of notice requiring the same to be remedied; or

(iii) if any order is made by any competent court or any resolution passed for the winding up or dissolution of the Issuer or an order is made for the Issuer's bankruptcy (or any analogous proceedings) save for the purposes of amalgamation, merger, consolidation, reorganisation or other similar arrangement on terms approved by the Bond Trustee or as otherwise permitted pursuant to these Conditions; or

(iv) if (1) any other proceedings are initiated against the Issuer under any applicable liquidation, bankruptcy, insolvency, composition, reorganisation, readjustment or other similar laws and such proceedings are not being disputed in good faith, or (2) an administrative receiver or other receiver, administrator or other similar official is appointed in relation to the Issuer or in relation to the whole or any substantial part of the undertaking or assets of the Issuer or (3)

an encumbrancer takes possession of the whole or any substantial part of the undertaking or assets of the Issuer or (4) a distress or execution or other process is levied or enforced upon or sued out against the whole or any substantial part of the undertaking or assets of the Issuer and in any of the foregoing cases (other than in relation to the circumstances described in (2) where no grace period shall apply) such order, appointment, possession or process (as the case may be) is not discharged or stayed or does not cease to apply within 14 days; or

(v) if the Issuer initiates or consents to judicial proceedings relating to itself (except in accordance with paragraph (iii) above) under any applicable liquidation, bankruptcy, insolvency, composition, reorganisation, readjustment or other similar laws or makes a conveyance or assignment for the benefit of its creditors generally; or

(vi) if the Issuer becomes insolvent or is adjudicated or found bankrupt; or

(vii) any acceleration under any Intercompany Loan Agreement.

''**Most Senior Class of Bonds**'' means (i) the Class A Bonds, Class B Bonds and Class R Bonds outstanding acting together in a single meeting whether by means of an Extraordinary Resolution or a request of at least one quarter of Principal Amount Outstanding of the holders thereof or (ii) if no Class A Bonds, Class B Bonds or Class R Bonds are outstanding, the outstanding Class C Bonds acting together in a single meeting whether by means of an Extraordinary Resolution or a request of Principal Amount Outstanding of at least one quarter of the holders thereof or (iii) if no Class A Bonds, Class B Bonds, Class R Bonds or Class C Bonds are outstanding, the outstanding Class D Bonds acting together in a single meeting whether by means of an Extraordinary Resolution or a request of Principal Amount Outstanding of at least one quarter of the holders thereof.

(b) Confirmation of No Issuer Event of Default

The Issuer shall provide written confirmation to the Bond Trustee, on an annual basis, that no Issuer Event of Default or other matter which is required to be brought to the Bond Trustee's attention has occurred.

(c) Enforcement of security

If the Bond Trustee gives written notice to the Issuer and the Issuer Security Trustee that the Bonds of all Sub-Classes of each Series are immediately due and repayable, the Issuer Security Trustee, acting on the instructions of the Issuer Instructing Group, shall enforce the Issuer Security as specified in Condition 4(d).

The Bond Trustee will not have any rights to call for repayment of the Bonds following the occurrence of an Issuer Event of Default except as provided in Condition 11(a) and the Issuer STID and enforcement of the Issuer Security by the Issuer Security Trustee will be subject to the provisions of the Issuer STID.

(d) Automatic Acceleration

In the event of (i) the acceleration of any of the Issuer's other obligations under the Issuer Transaction Documents and/or (ii) the acceleration of any DCC Secured Liabilities (as defined in the DCC STID), the Bonds of all Sub-Classes of every Class and Series are, and they shall immediately become, due and repayable, at their respective Principal Amounts Outstanding plus accrued and unpaid interest thereon.

12. Recourse Against Issuer

No Bondholder is entitled to take any action against the Issuer or, in the case of Class A Bondholders, 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 Issuer Security or to enforce any Bond Policy unless the Bond Trustee or the Issuer 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. The Issuer Security Trustee will act on the instructions of the Issuer Instructing Group pursuant to the Issuer STID and neither the Bond Trustee nor the Issuer Security Trustee shall be bound to take any such action unless it is indemnified and/or secured to its satisfaction.

Neither the Bond Trustee nor the Bondholders may institute against, or join any person in instituting against, the Issuer any bankruptcy, winding up, re-organisation, arrangement, insolvency or liquidation proceeding (except for the appointment of a receiver and manager pursuant to the terms of

the Issuer Deed of Charge and subject to the Issuer STID) or other proceeding under any similar law for so long as any Bonds are outstanding or for two years and a day after the latest Maturity Date on which any Bond of any Series is due to mature.

13. Prescription

Claims against the Issuer for payment in respect of the Bonds, Receipts or Coupons (which, for this purpose, shall not include Talons) shall be prescribed and become void unless made within ten years (in the case of principal) or five years (in the case of interest) from the appropriate Relevant Date (as defined in Condition 6(i)) in respect thereof.

14. Replacement of Bonds, Coupons, Receipts and Talons

If any Bearer Bond, Registered Bond, Receipt, Coupon or Talon is lost, stolen, mutilated, defaced or destroyed it may be replaced, subject to applicable laws and stock exchange requirements, at the specified office of the Principal Paying Agent or, as the case may be, the Registrar upon payment by the claimant of the expenses incurred in connection with such replacement and on such terms as to evidence, security, indemnity and otherwise as the Issuer may require. Mutilated or defaced Bonds, Receipts, Coupons or Talons must be surrendered before replacements will be issued.

15. Meetings of Bondholders, Modification, Waiver, Authorisation and Substitution

(a) Meetings of Bondholders, Modifications and Waiver

The Trust Deed contains provisions for convening meetings of Bondholders of a Sub-Class, Class or Classes to consider matters affecting their interests, including the modification of these Conditions, the Trust Deed and (in the case of Class A Bonds) the Bond Policies and any other Issuer Transaction Document to which the Bond Trustee is party. Any modification may (except in relation to any Entrenched Right or Reserved Matter of the Bond Trustee, subject, in the case of any of the Class A Bonds, to Entrenched Rights or Reserved Matters of any Financial Guarantor and subject to the provisions concerning ratification and/or meetings of particular combinations of Sub-Classes of Bonds as set out in Condition 15(b) and the Trust Deed, be made if sanctioned by a resolution passed at a meeting of such Bondholders duly convened and held in accordance with the Trust Deed by a majority of not less than three quarters of the votes cast (an ''**Extraordinary Resolution**'') of such Bondholders. Such a meeting may be convened by the Bond Trustee or the Issuer, or by the Bond Trustee upon the request in writing of the relevant Bondholders holding not less than one tenth of the aggregate Principal Amount Outstanding of the relevant outstanding Bonds.

The quorum at any meeting convened to vote on an Extraordinary Resolution will be two or more persons holding or representing not less than 50 per cent. of the aggregate Principal Amount Outstanding of the relevant outstanding Bonds or, at any adjourned meeting, two or more persons being or representing Bondholders, whatever the Principal Amount Outstanding of the relevant outstanding Bonds held or represented, provided however, that certain proposals (the ''**Basic Terms Modifications**'') in respect of the holders of any particular Sub-Class of Bonds means any proposal:

(i) to change any date fixed for payment of principal or interest in respect of such Sub-Class of Bonds, to reduce the amount of principal or interest payable on any date in respect of such Sub-Class of Bonds or (other than as specified in Conditions 7 and 8) to alter the method of calculating the amount of any payment in respect of such Sub-Class of Bonds on redemption or maturity;

(ii) other than pursuant to Condition 15(c), to effect the exchange, conversion or substitution of such Sub-Class of Bonds for, or the conversion of them into, shares, bonds or other obligations or securities of the Issuer or any other person or body corporate formed or to be formed;

(iii) to change the currency in which amounts due in respect of such Sub-Class of Bonds are payable other than pursuant to redenomination into euro pursuant to Condition 19;

(iv) to alter the Payments Priorities (as defined in the Master Framework Agreement) insofar as such alteration would affect such Sub-Class of Bonds;

(v) to alter the priority of redemption of such Sub-Class of Bonds;

(vi) in relation to any Sub-Class of Class A Bonds, to approve the release of the relevant Bond Policy or the substitution of the relevant Financial Guarantor;

(vii) to change the quorum required at any meeting or the majority required to pass an Extraordinary Resolution; or

(viii) to amend this definition or this Condition,

may be sanctioned only by an Extraordinary Resolution passed at a meeting of Bondholders of the relevant Sub-Class or Sub-Classes of Bonds at which two or more persons holding or representing not less than three-quarters or, at any adjourned meeting, one quarter of the aggregate Principal Amount Outstanding 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 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.

A meeting of such Bondholders will also have the power (exercisable by Extraordinary Resolution) to advise or instruct the Bond Trustee in connection with the exercise by the Bond Trustee of any of its rights, powers and discretions under the Issuer Transaction Documents including, to appoint any persons (whether Bondholders or not) as a committee to represent the interests of such Bondholders and to confer upon such committee any powers which such Bondholders could themselves exercise by Extraordinary Resolution and, where requested by the Bond Trustee, in relation to voting on Intercreditor Issues (as defined in Condition 15(d)) and in respect of the Reserved Matters and Entrenched Rights of the Bond Trustee.

(b) Relationship between Classes

In relation to each Sub-Class of Bonds:

(i) no Extraordinary Resolution involving a Basic Terms Modification that is passed by the holders of one Sub-Class of Bonds shall be effective unless it is sanctioned by an Extraordinary Resolution of the holders of each of the other Sub-Classes of Bonds (to the extent that there are Bonds outstanding in each such other Sub-Class); and

(ii) no Extraordinary Resolution (except in relation to an Intercreditor Issue or a vote under Condition 11(a)) to approve any matter other than a Basic Terms Modification of any Sub-Class of Bonds shall be effective unless it is sanctioned by an Extraordinary Resolution of the holders of each of the other Sub-Classes of Bonds ranking equally or senior to such Sub-Class (to the extent that there are Bonds outstanding ranking equally or senior to such Sub-Class), and for the avoidance of doubt as regards ranking, Class A Bonds, Class B Bonds and Class R Bonds will be considered to rank equally with each other, Class C Bonds are subordinate to the Class A Bonds, Class B Bonds and Class R Bonds and Class D Bonds are subordinate to the Class A Bonds, Class B Bonds, Class R Bonds and Class C Bonds;

provided that, in relation to a meeting of the holders of a Sub-Class of Bonds to sanction the Extraordinary Resolutions referred to in (i) and (ii) above, (1) the quorum for any such meeting shall be two or more persons holding or representing not less than 50 per cent. of the aggregate Principal Amount Outstanding of the relevant outstanding Bonds and (2) if the holders of any relevant Sub-Class of Bonds, having been invited to sanction a proposed Extraordinary Resolution, fail for want of quorum to pass or reject an Extraordinary Resolution sanctioning the proposed Extraordinary Resolution, such holders will be taken to have sanctioned the proposed matter. Conditions 15(a) and (b) in respect of meetings are subject to the further provisions of the Trust Deed.

(c) Modification, waiver and substitution

As more fully set out in the Trust Deed (and subject to the conditions and qualifications therein), the Bond Trustee may, without the consent of the Bondholders of any Sub-Class, concur with the Issuer or any other relevant parties in making (i) any modification of these Conditions, the Trust Deed, any Bond Policy or any Issuer Transaction Document which is of a formal, minor or technical nature or is made to correct a manifest error and (except as mentioned in the Trust Deed) (ii) any other modification and any waiver or authorisation of any breach or proposed breach of these Conditions, the Trust Deed, such Bond Policy or any such Issuer Transaction Document or other document which is in the opinion of the Bond Trustee not materially prejudicial to the interests of the Bondholders of that Sub-Class. Any such modification, waiver or authorisation shall be binding on the Bondholders of that Sub-Class, Class

or Classes 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 Sub-Class, Class or Classes as soon as practicable thereafter.

The Bond Trustee shall be entitled to assume that any such modification, 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.

As more fully set forth in the Issuer STID (and subject to the conditions and qualifications therein), the Bond Trustee may also agree with the Issuer, subject to the directions of the Issuer Instructing Group but without the consent of the relevant Bondholders of any Sub-Class, to the substitution of another corporation in place of the Issuer as principal debtor in respect of the Trust Deed and the Bonds of all Series and subject to the Class A Bonds continuing to carry the unconditional guarantee of the relevant Financial Guarantor.

(d) Voting by the Bondholders on Intercreditor Issues

In certain limited circumstances (as set out in the Issuer STID) the Bond Trustee shall be entitled to vote as the representative of Bondholders on intercreditor issues (''**Intercreditor Issues**''). The Bond Trustee shall vote on Intercreditor Issues (except in relation to any Basic Terms Modification) only in accordance with a direction by those holders of outstanding Bonds which constitute Qualifying Debt acting together whether by means of an Extraordinary Resolution or a request of at least one quarter of Principal Amount Outstanding of the holders thereof and shall not be obliged to vote unless it has been indemnified and/or secured to its satisfaction.

In accordance with the terms of the Issuer STID, if the Bond Trustee receives a Confirmation of Instruction (as defined in the Issuer STID) at any time before the date of a Bondholder meeting convened pursuant to this Condition 15(d) and the Trust Deed, it shall as soon as practicable notify the Bondholders that such meeting shall be cancelled and shall not be liable to any person for so doing.

16. Trustee Protections

(a) Trustee considerations

Subject to Condition 16(b), in connection with the exercise, under these Conditions, the Trust Deed, any Bond Policy or any Issuer Transaction Document, of its rights, powers, trusts, authorities and discretions (including, any modification, waiver, authorisation, determination or substitution), the Bond Trustee shall have regard to the interests of the holders of the Most Senior Class of 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 Sub-Classes of such Bonds, it shall consider the interests of the holders of the Sub-Class of the Most Senior Class of Bonds outstanding with the shortest dated maturity and will not have regard to the consequences of such exercise for the holders of other Classes or Sub-Classes 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 relating thereto 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 relating thereto of any such exercise.

(b) Exercise of rights

Except as otherwise provided in these Conditions and the Trust Deed, when exercising any rights, powers, trusts, authorities and discretions relating to or contained in the Conditions or the Trust Deed (other than in respect of any Entrenched Right or Reserved Matter or Basic Terms Modification, or in determining the occurrence of an Entrenched Right or Reserved Matter or Basic Terms Modification) which affects or relates to any Class A Bonds, the Bond Trustee shall only act with the consent of the relevant Financial Guarantor(s) in accordance with the provisions of the Issuer STID 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 Sub-Class of Bonds. Subject as provided in these Conditions and the Trust Deed, the Bond Trustee will exercise its rights under, or in relation to, the 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 11 only) been so requested in writing by the holders of at least 25 per cent. of the Outstanding Principal Amount of the relevant outstanding Bonds or (b) been so directed by an Extraordinary Resolution and (ii) been indemnified or furnished with security to its satisfaction.

17. Notices

Notices to holders of Registered Bonds will be posted to them at their respective addresses in the Register and deemed to have been given on the date of posting. Other notices to Bondholders will be valid if published in a leading daily newspaper having general circulation in London (which is expected to be the Financial Times and, if the Bonds which are listed on the Luxembourg Stock Exchange and the rules of that exchange so require, a leading newspaper having general circulation in Luxembourg (which is expected to be the *Luxemburger Wort*)). In addition, all notices to holders of Bonds (whether Bearer or Registered and whether Global Bonds or Definitive Bonds) will be published in such newspaper in Luxembourg. The Issuer shall also ensure that all notices are duly published in a manner which complies with the rules and regulations of any other listing authority, stock exchange and/or quotation system on which the Bonds are for the time being listed. Any such notice (other than to holders of Registered Bonds as specified above) shall be deemed to have been given on the date of such publication or, if published more than once or on different dates, on the first date on which publication is made. Couponholders and Receiptholders will be deemed for all purposes to have notice of the contents of any notice given to the holders of Bearer Bonds in accordance with this Condition 17.

So long as any Bonds are represented by Global Bonds notices in respect of those Bonds may be given by delivery of the relevant notice to Euroclear Bank S.A./N.V. as operator of the Euroclear System or Clearstream Banking, société anonyme or any other Relevant Clearing System as specified in the relevant Pricing Supplement for communication by them to entitled account holders in substitution for publication in a daily newspaper with general circulation in London. Such notices shall be deemed to have been received by the Bondholders 7 days after delivery to such clearing systems.

18. Indemnification of the Bond Trustee and Issuer Security Trustee

The Trust Deed and the Issuer STID contain provisions for indemnification of the Bond Trustee and the Issuer Security Trustee, respectively, and for their relief from responsibility, including provisions relieving them from taking any action including taking proceedings against the Issuer, any Financial Guarantor, and/or any other person or enforcing the Issuer Security unless indemnified and/or secured to their satisfaction. The Bond Trustee, the Issuer Security Trustee or any of their affiliates are entitled to enter into business transactions with the Issuer, any Financial Guarantor, the other Issuer Secured Creditors or any of their respective subsidiaries or associated companies without accounting for any profit resulting therefrom.

The Bond Trustee and the Issuer Security Trustee, in the absence of gross negligence or wilful default are exempted from any liability in respect of any loss, diminution in value or theft of all or any part of the Issuer Security, from any obligation to insure all or any part of the Issuer Security (including, in either such case, any documents evidencing, constituting or representing the same or transferring any rights, benefits and/or obligations thereunder) or to procure the same to be insured or monitoring the adequacy of any insurance arrangements.

19. European Economic And Monetary Union

(a) Notice of redenomination

The Issuer may, without the consent of the Bondholders, and on giving at least 30 days' prior notice to the Bondholders, the Issuer Instructing Group, the Bond Trustee, the Principal Paying Agent and the Registrar, as the case may be, designate a date (the "**Redenomination Date**"), being an Interest Payment Date under the Bonds falling on or after the date on which the United Kingdom becomes a Participating Member State.

(b) Redenomination

Notwithstanding the other provisions of these Conditions, with effect from the Redenomination Date:

(i) the Bonds of each Sub-Class denominated in sterling (the "**Sterling Bonds**") shall be deemed to be redenominated into euro in the denomination of euro 0.01 with a principal amount for each Bond equal to the principal amount of that Bond in sterling, converted into Euro at the rate for conversion of such currency into euro established by the Council of the European Union pursuant to the Treaty establishing the European Union, as amended, (including compliance with rules relating to rounding in accordance with European Community regulations), provided, however, that, if the Issuer determines, with the agreement of the Bond Trustee, that the then current market practice in respect of the redenomination into euro 0.01 of internationally offered securities is different from that 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 Luxembourg Stock Exchange and any other stock exchange (if any) on which the Bonds are then listed, (in the case of Bearer Bonds) the Principal Paying Agent and (in the case of registered Bonds) the Registrar of such deemed amendments;

(ii) if Bonds have been issued in definitive form:

(a) all Bonds denominated in sterling will become void with effect from the date (the "**Euro Exchange Date**") on which the Issuer gives notice (the "**Euro Exchange Notice**") to the Bondholders and the Bond Trustee that replacement Bonds denominated in euro are available for exchange (provided that such Bonds are available) and no payments will be made in respect thereof;

(b) the payment obligations contained in all Bonds denominated in sterling will become void on the Euro Exchange Date but all other obligations of the Issuer thereunder (including the obligation to exchange such Bonds in accordance with this Condition 19 (*European Economic and Monetary Union*) shall remain in full force and effect; and

(c) new Bonds denominated in euro will be issued in exchange for Sterling Bonds in such manner as the Principal Paying Agent or the Registrar, as the case may be, may specify and as shall be notified to the Bondholders in the Euro Exchange Notice;

(iii) all payments in respect of the Sterling Bonds (other than, unless the Redenomination Date is on or after such date as the sterling ceases to be a sub-division of the euro, payments of interest in respect of periods commencing before the Redenomination Date) will be made solely in euro by cheque drawn on, or by credit or transfer to a euro account (or any other account to which euro may be credited or transferred) maintained by the payee with, a bank in the principal financial centre of any Participating Member State; and

(iv) a Bond may only be presented for payment on a day which is a business day in the place of presentation.

(c) Interest

Following redenomination of the Bonds pursuant to this Condition 19 (*European Economic and Monetary Union*):

(i) where Sterling Bonds have been issued in definitive form, the amount of interest due in respect of the Sterling Bonds will be calculated by reference to the aggregate principal amount of the Sterling Bonds presented for payment by the relevant holder and the amount of such payment shall be rounded down to the nearest euro 0.01; and

(ii) the amount of interest payable in respect of each Sub-Class of Sterling Bonds for any Interest Period shall be calculated by applying the Interest Rate applicable to the Sub-Class of Bonds denominated in euro ranking *pari passu* to the relevant Sub-Class.

20. Miscellaneous

(a) Governing Law

The Trust Deed, the Issuer Deed of Charge, the Issuer STID, the Bonds, the Coupons, the Receipts, the Talons (if any), the relevant Bond Policy (if any) and the other Issuer Transaction Documents are governed by and shall be construed in accordance with the laws of England and Wales.

(b) Third Party Rights

No person shall have any right to enforce any term or condition of the Bonds or the Trust Deed under the UK Contracts (Rights of Third Parties) Act 1999.

FORMS OF THE BONDS

Form and Exchange — Bearer Bonds

Each Sub-Class of Bonds initially issued in bearer form will be issued either as a temporary global bond (the "**Temporary Global Bond**"), without Coupons or Talons attached, or a permanent global bond (the "**Permanent Global Bond**"), without interest Coupons or Talons attached, in each case as specified in the relevant Pricing Supplement. Each Temporary Global Bond or, as the case may be, Permanent Global Bond (each a "**Global Bond**") will be delivered prior to the Issue Date of the relevant Sub-Class of the Bonds to a depositary or a common depositary for Euroclear and/or Clearstream, Luxembourg and/or any other relevant clearing system.

The relevant Pricing Supplement will also specify whether United States Treasury Regulation §1.163-5(c)(2)(i)(C) (the "**TEFRA C Rules**") or United States Treasury Regulation §1.163-5(c)(2)(i)(D) (the "**TEFRA D Rules**") are applicable in relation to the Bonds.

Temporary Global Bond exchangeable for Permanent Global Bond

If the relevant Pricing Supplement specifies the form of Bonds as being represented by "Temporary Global Bond exchangeable for a Permanent Global Bond", then the Bonds will initially be in the form of a Temporary Global Bond which will be exchangeable, in whole or in part, for interests in a Permanent Global Bond, without Coupons or Talons attached, not earlier than 40 days after the Issue Date of the relevant Sub-Class of the Bonds upon certification as to non-U.S. beneficial ownership. No payments will be made under the Temporary Global Bond unless exchange for interests in the Permanent Global Bond is improperly withheld or refused. In addition, payments of principal and interest in respect of the Bonds cannot be collected without such certification of non-U.S. beneficial ownership.

Whenever any interest in the Temporary Global Bond is to be exchanged for an interest in a Permanent Global Bond, the Issuer shall procure (in the case of first exchange) the prompt delivery (free of charge to the bearer) of such Permanent Global Bond, duly authenticated, to the bearer of the Temporary Global Bond or (in the case of any subsequent exchange) an increase in the principal amount of the Permanent Global Bond in accordance with its terms against:

- presentation and (in the case of final exchange) surrender of the Temporary Global Bond at the Specified Office (as defined in the Paying Agency Agreement) of the Paying Agent; and
- receipt by the Paying Agent of a certificate or certificates of non-U.S. beneficial ownership issued by Euroclear and/or Clearstream, Luxembourg and/or any other relevant clearing system,

within 60 days of the bearer requesting such exchange.

The principal amount of the Permanent Global Bond shall be equal to the aggregate of the principal amounts specified in the certificates of non-U.S. beneficial ownership; *provided, however*, that in no circumstances shall the principal amount of the Permanent Global Bond exceed the aggregate initial principal amount of the Temporary Global Bond and any Temporary Global Bond representing a fungible Sub-Class of Bonds with the Sub-Class of Bonds represented by the first Temporary Global Bond.

The Permanent Global Bond will be exchangeable in whole, but not in part, for Bonds in definitive form ("**Definitive Bonds**"):

- on the expiry of such period of notice as may be specified in the relevant Pricing Supplement; or
- at any time, if so specified in the relevant Pricing Supplement; or
- if the relevant Pricing Supplement specifies "in the limited circumstances described in the Permanent Global Bond", then if (a) Euroclear or Clearstream, Luxembourg or any other relevant clearing system is closed for business for a continuous period of 14 days (other than by reason of legal holidays) or announces an intention permanently to cease business or (b) any of the circumstances described in Condition 11(a) (Issuer Events of Default) occurs; or

- the Issuer certifies to the Bond Trustee that it has or will, on the next payment date for interest or principal, become subject to adverse tax consequences which would not be suffered if the Bonds are not represented by a Permanent Global Bond.

Whenever the Permanent Global Bond is to be exchanged for Definitive Bonds, the Issuer shall procure the prompt delivery (free of charge to the bearer) of such Definitive Bonds, duly authenticated and with Coupons and Talons attached (if so specified in the relevant Pricing Supplement), in an aggregate principal amount equal to the principal amount of the Permanent Global Bond to the bearer of the Permanent Global Bond against the surrender of the Permanent Global Bond at the Specified Office of the Paying Agent within 60 days of the bearer requesting such exchange but not earlier than 40 days after the Issue Date of such Bonds.

Temporary Global Bond exchangeable for Definitive Bonds

If the relevant Pricing Supplement specifies the form of Bonds as being "Temporary Global Bond exchangeable for Definitive Bonds" and also specifies that the TEFRA C Rules are applicable or that neither the TEFRA C Rules or the TEFRA D Rules are applicable, then the Bonds will initially be in the form of a Temporary Global Bond which will be exchangeable, in whole but not in part, for Definitive Bonds not earlier than 40 days after the issue date of the relevant Sub-Class of the Bonds.

If the relevant Pricing Supplement specifies the form of Bonds as being "Temporary Global Bond exchangeable for Definitive Bonds" and also specifies that the TEFRA D Rules are applicable, then the Bonds will initially be in the form of a Temporary Global Bond which will be exchangeable, in whole or in part, for Definitive Bonds not earlier than 40 days after the issue date of the relevant Sub-Class of the Bonds upon certification as to non-U.S. beneficial ownership. Principal and interest payments in respect of the Bonds cannot be collected without such certification of non-U.S. beneficial ownership.

Whenever the Temporary Global Bond is to be exchanged for Definitive Bonds, the Issuer shall procure the prompt delivery (free of charge to the bearer) of such Definitive Bonds, duly authenticated and with Coupons and Talons attached (if so specified in the relevant Pricing Supplement), in an aggregate principal amount equal to the principal amount of the Temporary Global Bond so exchanged to the bearer of the Temporary Global Bond against the presentation (and in the case of final exchange, surrender) of the Temporary Global Bond at the Specified Office of the Paying Agent within 60 days of the bearer requesting such exchange but not earlier than 40 days after the Issue Date of such Bonds.

Permanent Global Bond exchangeable for Definitive Bonds

If the relevant Pricing Supplement specifies the form of Bonds as being "Permanent Global Bond exchangeable for Definitive Bonds", then the Bonds will initially be in the form of a Permanent Global Bond which will be exchangeable in whole, but not in part, for Definitive Bonds:

- on the expiry of such period of notice as may be specified in the relevant Pricing Supplement; or

- at any time, if so specified in the relevant Pricing Supplement; or

- if the relevant Pricing Supplement specifies "in the limited circumstances described in the Permanent Global Bond", then if (a) Euroclear or Clearstream, Luxembourg or any other relevant clearing system is closed for business for a continuous period of 14 days (other than by reason of legal holidays) or announces an intention permanently to cease business or (b) any of the circumstances described in Condition 11(a) (*Issuer Events of Default*) occurs; or

- the Issuer certifies to the Bond Trustee that it has or will, on the next payment date for interest or principal, become subject to adverse tax consequences which would not be suffered if the Bonds are not represented by a Permanent Global Bond.

Whenever the Permanent Global Bond is to be exchanged for Definitive Bonds, the Issuer shall procure the prompt delivery (free of charge to the bearer) of such Definitive Bonds, duly authenticated and with Coupons and Talons attached (if so specified in the relevant Pricing Supplement), in an aggregate principal amount equal to the principal amount of the Permanent Global Bond to the bearer of the Permanent Global Bond against the surrender of the Permanent Global Bond at the Specified Office of the Paying Agent within 60 days of the bearer requesting such exchange but not earlier than 40 days after the Issue Date of such Bonds.

Conditions applicable to the Bonds

The Conditions applicable to any Definitive Bond will be endorsed on that Bond and will consist of the Conditions set out under "*Terms and Conditions of the Bonds*" above and the provisions of the relevant Pricing Supplement which supplement, amend, vary and/or replace those Conditions.

The Conditions applicable to any Global Bond will differ from those Conditions which would apply to the Definitive Bond to the extent described under "*Provisions Relating to the Global Bonds*".

Legend concerning United States persons

Global Bonds and Definitive Bonds and any Coupons and Talons appertaining thereto will bear a legend to the following effect:

"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 in such legend provide that a United States person who holds a Bond, Coupon or Talon will generally not be allowed to deduct any loss realised on the sale, exchange or redemption of such Bond, Coupon or Talon and any gain (which might otherwise be characterised as capital gain) recognised on such sale, exchange or redemption will be treated as ordinary income.

Form and Exchange — Global Bond Certificates

Global Certificates

Registered Bonds held in Euroclear and/or Clearstream, Luxembourg and/or any other clearing system will be represented by a Global Bond Certificate which will be registered in the name of a nominee for, and deposited with, a depositary for Euroclear and/or Clearstream, Luxembourg and/or such other relevant clearing system.

Exchange

The Global Bond Certificate will become exchangeable in whole, but not in part, for Individual Bond Certificates if (a) Euroclear or Clearstream, Luxembourg and/or any other relevant clearing system is closed for business for a continuous period of 14 days (other than by reason of legal holidays) or announces an intention permanently to cease business, (b) any of the circumstances described in Condition 11(a) (*Issuer Events of Default*) occurs, (c) at any time at the request of the registered Holder if so specified in the Pricing Supplement or (d) the Issuer certifies to the Bond Trustee that it has or will, on the next payment date for interest or principal, become subject to adverse tax consequences which would not be suffered if the Bonds are not represented by a Global Bond Certificate.

Whenever the Global Bond Certificate is to be exchanged for Individual Bond Certificates, such will be issued in an aggregate principal amount equal to the principal amount of the Global Bond Certificate within ten business days of the delivery, by or on behalf of the registered Holder of the Global Bond Certificate to the Registrar or the Transfer Agents (as the case may be) of such information as is required to complete and deliver such Individual Bond Certificates (including the names and addresses of the persons in whose names the Individual Bond Certificates are to be registered and the principal amount of each such person's holding) against the surrender of the Global Bond Certificate at the specified office of the Registrar or the Transfer Agent (as the case may be). Such exchange will be effected in accordance with the provisions of the Paying Agency Agreement and the regulations concerning the transfer and registration of Bonds scheduled thereto and, in particular, shall be effected without charge to any holder, but against such indemnity as the Registrar or the Transfer Agents (as the case may be) may require in respect of any tax or other duty of whatsoever nature which may be levied or imposed in connection with such exchange.

Rights Against Issuer

Under the Trust Deed, persons shown in the records of Euroclear and/or Clearstream, Luxembourg and/or any other relevant clearing system as being entitled to interests in the Bonds will (subject to the terms of the Trust Deed and the Issuer STID) acquire directly against the Issuer all those rights to which they would have been entitled if, immediately before the Global Bond or Global Bond Certificate became void, they had been the registered Holders of Bonds in an aggregate principal amount equal to the principal amount of Bonds they were shown as holding in the records of Euroclear, Clearstream, Luxembourg or any other relevant clearing system (as the case may be).

PROVISIONS RELATING TO THE BONDS WHILE IN GLOBAL FORM

Clearing System Accountholders

References in the Conditions of the Bonds to "**Bondholder**" are (other than in the case of payment) references to the person shown in the records of the relevant clearing system as the holder of the Global Bond or Global Bond Certificate.

Each of the persons shown in the records of Euroclear and/or Clearstream, Luxembourg and/or any other relevant clearing system, as the case may be, as being entitled to an interest in a Global Bond or a Global Bond Certificate (each an "**Accountholder**") must look solely to Euroclear and/or Clearstream, Luxembourg and/or such other relevant clearing system (as the case may be) for such Accountholder's share of each payment made by the Issuer or, in the case of Class A Bonds, the relevant Financial Guarantor, to such Accountholder and in relation to all other rights arising under the Global Bond or Global Bond Certificate. The extent to which, and the manner in which, Accountholders may exercise any rights arising under a Global Bond or Global Bond Certificate will be determined by the respective rules and procedures of Euroclear, Clearstream, Luxembourg and any other relevant clearing system (as the case may be) from time to time. For so long as the relevant Bonds are represented by a Global Bond or Global Bond Certificate, Accountholders shall have no claim directly against the Issuer or, in the case of Class A Bonds, the relevant Financial Guarantor in respect of payments due under the Bonds and such obligations of the Issuer and, in the case of Class A Bonds, the relevant Financial Guarantor will be discharged by payment to the bearer of the Global Bond or the registered holder of the Global Bond Certificate, as the case may be.

Amendment to Conditions

Global Bonds will contain provisions that apply to the Bonds which they represent, some of which modify the effect of the Conditions of the Bonds as set out in this Information Memorandum. The following is a summary of certain of those provisions:

- *Meetings:* The holder of a Global Bond or Global Bond Certificate shall be treated as being two persons for the purposes of any quorum requirements of a meeting of Bondholders and, at any such meeting, the holder of a Global Bond or Global Bond Certificate shall be treated as having one vote in respect of each minimum denomination of Bonds for which such Global Bond or Global Bond Certificate may be exchanged.

- *Cancellation:* Cancellation of any Bond represented by a Global Bond or Global Bond Certificate that is required by the Conditions to be cancelled (other than upon its redemption) will be effected by reduction in the principal amount of the relevant Global Bond or Global Bond Certificate.

- *Notices:* So long as any Bonds are represented by a Global Bond or Global Bond Certificate and such Global Bond or Global Bond Certificate is held on behalf of Euroclear, Clearstream, Luxembourg or any other relevant Clearing System, notices to the Bondholders may be given, subject always to listing requirements, by delivery of the relevant notice to Euroclear, Clearstream, Luxembourg or any other relevant Clearing System for communication by it to entitled Accountholders in substitution for publication as provided in the Conditions provided that, in any case, all such notices shall be published in a leading daily newspaper having general circulation in Luxembourg in accordance with Condition 17.

PRO FORMA PRICING SUPPLEMENT

The Pricing Supplement in respect of each Sub-Class of Bonds will be substantially in the following form, duly supplemented, varied or amended (if necessary) and completed to reflect the particular terms of the relevant Bonds and their issue. Text in this section appearing in italics does not form part of the form of the Pricing Supplement but denotes directions for completing the Pricing Supplement.

Pricing Supplement dated [*date*]

Dwr Cymru (Financing) Limited

Issue of *[Sub-Class [●] (delete as appropriate)] [Aggregate Nominal Amount of Sub-Class] [Title of Bonds]*

[(*if Class A Bonds issued including the following:*):
unconditionally and irrevocably guaranteed as to scheduled payments of principal and interest by

[Name of Financial Guarantor]

This document constitutes the Pricing Supplement relating to the issue of [indicate relevant Sub-Class] Bonds described herein. Terms used herein shall be deemed to be defined as such for the purposes of the Conditions set forth in the Information Memorandum dated [●] 2001. This Pricing Supplement must be read in conjunction with such Information Memorandum.

The Bonds constitute longer term debt securities issued in accordance with regulations made under section 4 of the UK Banking Act 1987.

The Issuer is not an authorised institution or a European authorised institution (as such terms are defined in the Banking Act 1987 (Exempt Transactions) Regulations 1997).

[*Note: include equivalent above paragraph for Financial Guarantor if Class A Bonds.*]

[Repayment of the principal and payment of any interest or premium in connection with the Bonds has not been guaranteed.]

[*Note: include above paragraph if not Class A Bonds being described in the Pricing Supplement.*]

The Issuer (a) has complied with its obligations under the listing rules of the Luxembourg Stock Exchange in relation to the admission to and continuing listing of the Programme and of any previous issues made by it under the Programme and listed on the same exchange; (b) confirms that it will have complied with its obligations under the listing rules of the Luxembourg Stock Exchange in relation to the admission to listing of the Bonds by the time when the Bonds are so admitted; (c) has not, since the last publication of information in compliance with the listing rules of the Luxembourg Stock Exchange about the Programme, any previous issues made by it under the Programme and listed on the Luxembourg Stock Exchange, or the Bonds, having made all reasonable enquiries, become aware of any change in circumstances which could reasonably be regarded as significantly and adversely affecting its ability to meet its obligations as issuer in respect of the Bonds as they fall due; and (d) has complied and will continue to comply with its obligations under the Banking Act 1987 (Exempt Transactions) Regulations 1997 to lodge all relevant information in relation to the Bonds with the London Stock Exchange.

[*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 sub-paragraphs. Italics denote directions for completing the Pricing Supplement.]*

1.	(i) Issuer:	**Dwr Cymru (Financing) Limited**
	(ii) Financial Guarantor:	[Name of Financial Guarantor] *[delete if not Class A Bonds]*
2.	(i) Series Number:	[●]
	(ii) Sub-Class Number: *(If fungible with an existing Sub-Class, details of that Sub-Class, including the date on which the Bonds become fungible).*	[●]
3.	Relevant Currency:	[●]
4.	Aggregate Nominal Amount:	
	(i) Series:	[●]
	(ii) Sub-Class:	[●]

5.	(i) Issue Price:	[●] per cent. of the Aggregate Nominal Amount [plus accrued interest from [*insert date*]] *(in the case of fungible issues only, if applicable)*]
	(ii) Net proceeds:	[●]
6.	Specified Denominations:	[●]
7.	(i) Issue Date:	[●]
	(ii) Interest Commencement Date (if different from the Issue Date):	[●]
8.	Maturity Date:	[*specify date or* (*for Floating Rate Bonds) Interest Payment Date falling in [the relevant month and year]*]
9.	Interest Basis:	[Fixed Rate/Floating Rate/Indexed]
10.	Redemption/Payment Basis:	Applicable – Condition 8 [Instalments]
11.	Change of Interest or Redemption/Payment Basis:	[*Specify details of any provision for convertibility of Bonds into another interest or redemption/payment basis*]
12.	Put/Call Options:	Call option – see below
13.	(i) Status and Ranking:	[*if Class A Bonds, Class B Bonds or Class R Bonds:*] the Class A Bonds, Class B Bonds and Class R Bonds rank *pari passu* among each other in terms of interest and principal payments and rank in priority to the Class C Bonds and Class D Bonds; [*if Class C Bonds:*] the Class C Bonds rank *pari passu* among each other and are subordinated in terms of interest and principal payments to the Class A Bonds, Class B Bonds and Class R Bonds and rank in priority to the Class D Bonds; [*if Class D Bonds:*] the Class D Bonds rank *pari passu* among each other and are subordinated in terms of principal and interest payments to the Class A Bonds, Class B Bonds, Class R Bonds and Class C Bonds.
	(ii) Status of the Guarantee:	[*if Class A Bonds:*] [The Bond Policy will rank *pari passu* with all unsecured obligations of the Financial Guarantor.]
	(iii) FG Event of Default (if not MBIA)	[*Specify for Financial Guarantor*]
14.	Listing:	[Luxembourg] [*and other exchanges as applicable*]
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) Interest Rate:	[●] per cent. per annum [payable [annually / semi-annually / quarterly / monthly] in arrear]
	(ii) Interest Payment Date(s):	[●] in each year
	(iii) First Interest Payment Date:	[●]
	(iv) Fixed Coupon Amount[(s)]:	[●] per [●] in Nominal Amount
	(v) Broken Amount(s):	[*Insert particulars of any initial or final broken interest amounts which do not correspond with the Fixed Coupon Amount[(s)]*]
	(vi) Day Count Fraction:	[Actual/Actual ISMA] [Actual/365 or Actual/Actual] [Actual/365 Fixed] [Actual/360] [30/360 or 360/360 or Bond Basis] [30E/360 or Eurobond Basis]
	(vii) Other terms relating to the method of calculating interest for Fixed Rate Bonds:	[*Not Applicable/give details]*
	(viii) Benchmark Gilt	[●]
17.	Floating Rate Bond Provisions	[Applicable/Not Applicable] (*If not applicable, delete the remaining sub-paragraphs of this paragraph*)
	(i) Interest Payment Date(s):	[●]
	(ii) First Interest Payment Date:	[●]
	(iii) Business Day Convention:	[Following Business Day Convention/ Modified Following Business Day Convention/ Preceding Business Day Convention/ other (*give details)*]
	(iv) Manner in which the Interest Rate(s) is/are to be determined:	[Screen Rate Determination/ISDA Determination/other (*give details)*]
	(v) Party responsible for calculating the Interest Rate(s) and Interest Amount(s) (if not the Agent Bank):	[Not Applicable]
	(vi) Screen Rate Determination:	
	– Relevant Rate:	[●]
	– Interest Determination Date(s):	[●]
	– Page:	[●]
	(vii) ISDA Determination:	
	– Floating Rate Option:	[●]
	– Designated Maturity:	[●]
	– Reset Date:	[●]
	(viii) Margin(s):	[+/-][●] per cent. per annum
	(ix) Minimum Interest Rate:	[Not Applicable]
	(x) Maximum Interest Rate:	[Not Applicable]

	(xi)	Day Count Fraction:	[Actual/Actual ISMA] [Actual/365 or Actual/Actual] [Actual/365 Fixed] [Actual/360] [30/360 or 360/360 or Bond Basis] [30E/360 or Eurobond Basis]
	(xii)	Additional Business Centre(s):	[●]
	(xiii)	Fall back provisions, rounding provisions, denominator and any other terms relating to the method of calculating interest on Floating Rate Bonds, if different from those set out in the Conditions:	[●]
	(xiv)	Relevant Financial Centre:	[●]
	(xv)	Representative Amount:	[●]
18.		Zero Coupon Bond Provisions	[Not Applicable/Applicable (*give details*)]
19.		Indexed Bond Provisions	[Applicable/Not Applicable] (*If not applicable, delete the remaining subparagraphs of this paragraph*)
	(i)	Index/Formula:	UK Retail Price Index
	(ii)	Interest Rate:	[●]
	(iii)	Calculation Agent responsible for calculating the interest due:	Agent Bank
	(iv)	Provisions for determining Coupon where calculation by reference to Index and/or Formula is impossible or impracticable:	Applicable – Condition 7(c) and Condition 7(e)
	(v)	Interest Payment Dates:	[●]
	(vi)	First Interest Payment Date:	[●]
	(vii)	Business Day Convention:	[Following Business Day/Modified Following Business Day /Preceding Business Day/other *(give details)*]
	(viii)	Minimum Indexation Factor:	[Not Applicable/*specify*]
	(ix)	Maximum Indexation Factor:	[Not Applicable/*specify*]
	(x)	Limited Indexation Months(s):	[●]
	(xi)	Reference Gilt	[●]
	(xii)	Day Count Fraction:	[Actual/Actual ISMA] [Actual/365 or Actual/Actual] [Actual/365 Fixed] [Actual/360] [30/360 or 360/360 or Bond Basis] [30E/360 or Eurobond Basis]
20.		Dual Currency Bond Provisions	Not Applicable

PROVISIONS RELATING TO REDEMPTION

21. Call Option	Applicable – Condition 8 *(If not applicable, delete the remaining sub-paragraphs of this paragraph)*
(i) Optional redemption date(s):	Yes. [In the case of Floating Rate Bonds, not before [●] and at a premium of [●], if any.]
(ii) Optional redemption amount(s) and method, if any, of calculation of such amount(s):	[●]
(iii) If redeemable in part:	
(a) Minimum Redemption Amount:	[Not Applicable]
(b) Maximum Redemption Amount:	[Not Applicable]
(iv) Notice period (if other than as set out in the Conditions):	[Not Applicable]
22. Put Option	Not Applicable
23. Redemption Amount	[Par/other/see Appendix]

GENERAL PROVISIONS APPLICABLE TO THE BONDS

24. Form of Bonds:	[Bearer/Registered]
(i) If Bearer Bonds:	[Temporary Global Bond exchangeable for a Permanent Global Bond which is exchangeable for Definitive Bonds on [●] days' notice/at any time/in the limited circumstances specified in the Permanent Global Bond/for tax reasons.] [Temporary Global Bond exchangeable for Definitive Bonds on [●] days' notice.] [Permanent Global Bond exchangeable for Definitive Bonds on [●] days' notice/at any time/in the limited circumstances specified in the Permanent Global Bond/for tax reasons.]
(ii) If Registered Bonds:	[Regulation S Global Registered Bond Certificate exchangeable for Regulation S Individual Registered Bond Certificates]
25. Relevant 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 item 17(iii) and 19 (vi) relate*]
26. Talons for future Coupons or Receipts to be attached to Definitive Bonds (and dates on which such Talons mature):	[Yes/No. *If yes, give details*]
27. Details relating to Partly Paid Bonds:	[Not Applicable]
28. Details relating to Instalment Bonds:	[Applicable/Not Applicable/*give details*]
(i) Instalment Date:	[●]
(ii) Instalment Amount:	[●]
29. Redenomination, renominalisation and reconventioning provisions:	[Not Applicable/The provisions in Condition 19 apply]

30.	Consolidation provisions:	[Not Applicable]
31.	Other terms or special conditions:	[Not Applicable/*give details*]
32.	TEFRA rules:	[TEFRA C]/[TEFRA D]

INTERCOMPANY LOAN TERMS

33.	Interest rate on relevant Term Advance/ Revolving Advance:	[●]
34.	Term of relevant Term Advance/Revolving Advance:	[●]
35.	Repayment Schedule for relevant Term Advance:	[●]
36.	Other relevant provisions:	[●]

DISTRIBUTION

37.	(i) If syndicated, names of Managers:	[Not Applicable/*give names]*
	(ii) Stabilising Manager (if any):	[Not Applicable/*give name]*
38.	If non-syndicated, name of Dealer:	[Not Applicable/*give name]*
39.	Additional selling restrictions:	[Not Applicable/*give details]*

OPERATIONAL INFORMATION

40.	ISIN Code:	[●]
41.	Common Code:	[●]
42.	Any Relevant Clearing System(s) other than Euroclear and Clearstream, Luxembourg and the relevant identification number(s):	[Not Applicable/*give name(s) and number(s)*]
43.	Delivery:	Delivery [against/free of] payment
44.	Paying Agent(s), Transfer Agents, Registrar and Agent Bank:	[●]

LISTING APPLICATION

This Pricing Supplement comprises the details required to list the issue of Bonds described herein pursuant to the listing of the Programme for the issuance of up to £3,000,000,000 Guaranteed Asset-Backed Bonds and £3,000,000,000 Asset-Backed Bonds including up to £200,000,000 Class R Asset-Backed Bonds financing Dŵr Cymru Cyfyngedig.

RESPONSIBILITY

The Issuer accepts responsibility for the information contained in this Pricing Supplement [save for the [Financial Guarantor] Information]. [The Financial Guarantor accepts responsibility for the [Financial Guarantor] Information contained in this Pricing Supplement] (*delete if not applicable*).

Signed on behalf of the Issuer:

By: ....

Duly authorised

Signed on behalf of the Financial Guarantor [*If in relation to Class A Bonds*]:

By: ....

Duly authorised

CHAPTER 7

MBIA AND THE BOND POLICIES

MBIA ASSURANCE S.A.

General

MBIA is a *société anonyme* that was created and incorporated under French law on 3 May 1990. MBIA's corporate charter expires on 3 May 2089. MBIA's principal activity is the guarantee of financial obligations. MBIA is subject to the provisions of the French law of 24 July 1966 on commercial companies. Furthermore, MBIA is licensed in the French Republic, under the terms of Article L-321-1 of the French Insurance Code ("**Code des Assurances**"), to carry out operations of the type corresponding to Branch 15 Guarantee listed in Article R-321-1 of the aforementioned Code (Journal Officiel dated 28 March 1991). MBIA is under the supervision of the Commission de Contrôle des Assurances. Its registration number is the Commercial Register (Paris Register of Trade and Companies) No. B377883293 (98 B 05130). MBIA has its head office in Paris at 112, Avenue Kléber, 75116 Paris, France.

MBIA has used the provisions of the Third Non-life Insurance Directive of the European Community Directive No. 92-49-EE1 (the "**Insurance Directive**") to operate in the United Kingdom both on a services and a branch basis. It was established as an overseas company under number FC020116 and as a branch under number BR003789 in England and Wales under Schedule 21A to the UK Companies Act 1985 (the "**Companies Act**") on 10 February 1997. MBIA's business in the United Kingdom is to a limited extent subject to supervision by the Financial Services Authority. Its branch office is located at 1 Great St Helen's, 2nd Floor, London, EC3A 6HX, United Kingdom.

Business and Financial Structure

MBIA is licensed to do business in, and is subject to regulation under the laws of, the French Republic. MBIA has used the provisions of the Insurance Directive to operate in the United Kingdom both on a services and a branch basis and is to a limited extent subject to supervision by the Financial Services Authority. MBIA is a 99.99 per cent. owned subsidiary of MBIA Insurance Corporation. MBIA Insurance Corporation is the principal operating subsidiary of MBIA Inc., a New York Stock Exchange listed company. MBIA Inc. is not obliged to pay the debts of, or claims against, MBIA Insurance Corporation or MBIA.

MBIA is engaged primarily in carrying out insurance and reinsurance transactions of any kind authorised by the Commission de Contrôle des Assurances, excepting insurance transactions involving commitments, the performance of which depends on human life, but including particularly guarantee transactions, and notably, insuring the repayment of financial or other contractual obligations entered into by local governments, other public entities, companies, trusts and other commercial entities as well as any ancillary activities. MBIA may, to this purpose, make any investment and acquire any stake, in France and/or abroad, through the acquisition of a participating interest or securities, contributions in cash or in kind, subscription to any issue of shares or bonds, loans or credits; and may, to this end, borrow and make use of any means of financing it may choose and pledge such investments or interests as it sees fit. MBIA may carry out in France and/or abroad any industrial, commercial, financial or real estate operations that may be linked, directly or indirectly, to the above activities or are likely to facilitate the development thereof within the scope of the legislation specific to insurance companies.

Business – Developments

Over the past 4 years, MBIA has guaranteed a variety of bond issues including issues by French and Spanish government entities, securitisations and structured transactions.

Capitalisation and Indebtedness of MBIA

As at 31 December 2000 and 31 December 1999, the capitalisation and indebtedness of MBIA were as follows:

MBIA – Capitalisation and Indebtedness Table (French Francs (''FF'') thousands)[1]

	Audited 31 December 2000	Audited 31 December 1999
Indebtedness		
– Funds held[2]	25,499	39,506
Stockholders' Equity		
– Common stock, par value FF 100 per share: 1,750,000 authorised and issued shares (fully paid)	175,000	175,000
– Retained Earnings	37,250	38,271
Total Stockholders Equity	212,250	213,271
Total Capitalisation and Indebtedness[3]	237,749	252,777

1 This Capitalisation and Indebtedness Table has been prepared in accordance with generally accepted accounting principles in France. Save as set out in the Table, MBIA did not at the relevant dates have any loan capital outstanding or created but unissued, term loans or any other borrowings in the nature of borrowing, including bank overdrafts and liabilities under acceptances or acceptance credits, mortgages, charges, finance lease commitments, hire purchase obligations or guarantees, or contingent liabilities.

2 Represents security deposits held by MBIA in respect of insured transactions relating to two past securitisations. There is a corresponding asset of equal value on the MBIA balance sheet.

3 There has been no material change in the authorised and issued share capital, and in the capitalisation and indebtedness of MBIA since the date of this Capitalisation and Indebtedness Table, and MBIA has no material contingent liabilities or guarantees.

Relationship between MBIA and MBIA Insurance Corporation

MBIA Insurance Corporation and MBIA have entered into (i) a reinsurance agreement providing for MBIA Insurance Corporation's reinsurance of the risks incurred by MBIA (the ''**Reinsurance Agreement**'') dated 1 January 1993 and (ii) an agreement dated 1 November 1991 whereby MBIA Insurance Corporation agrees to maintain the net worth of MBIA, to remain its sole shareholder and not to pledge its shares of MBIA (as amended, the ''**Net Worth Maintenance Agreement**''). Under the Reinsurance Agreement, MBIA Insurance Corporation agrees to reimburse MBIA, on an excess of loss basis, for losses incurred in each calendar year for net retained insurance liability. MBIA Insurance Corporation shall reimburse MBIA for the amount of MBIA's losses paid in each calendar year which amount is in the aggregate in excess of an amount equal to the greater of: (1) US$500,000 or (2) 40 per cent. of MBIA's net earned premium income for that same calendar year. The liability of MBIA Insurance Corporation shall not exceed US$100,000,000 in any one calendar year.

Under the Net Worth Maintenance Agreement, MBIA Insurance Corporation agrees to maintain a minimum capital and surplus position of FF 30 million, or such greater amount as shall be required now or in the future by French law or French regulatory authorities; provided however, any contributions to MBIA for such purpose shall not exceed 35 per cent. of MBIA Insurance Corporation's policyholders' surplus on an accumulated basis as determined by the laws of the State of New York.

MBIA has no subsidiaries.

Class A Bondholders should note that the Net Worth Maintenance Agreement between MBIA and MBIA Insurance Corporation and the Reinsurance Agreement (together, the ''MBIA Assurance Agreements'') are entered into for the benefit of MBIA and are not, and should not be regarded as, guarantees by MBIA Insurance Corporation of the payment of any indebtedness, liability or obligations of the Issuer, the Class A Bonds or the Bond Policies of MBIA. Bondholders should note that MBIA's ability to perform its obligations under its Bond Policies and to maintain its current rating substantially depends on the ability of MBIA Insurance Corporation under the MBIA Assurance Agreement.

Information in this Information Memorandum concerning MBIA Insurance Corporation is provided for background purposes only in view of the importance to MBIA of the MBIA Assurance Agreements. It does not imply that the MBIA Assurance Agreements are

guarantees for the benefit of Class A Bondholders. Payments of principal and of interest on the Class A Bonds will be guaranteed by MBIA pursuant to its Bond Policies and will not be additionally guaranteed by MBIA Insurance Corporation.

Bondholders should note that MBIA's ability to perform its obligations under its Bond Policies and to maintain its current rating substantially depend on the ability of MBIA Insurance Corporation to perform its obligations under the MBIA Assurance Agreements.

The MBIA Assurance Agreements are agreements solely between MBIA and MBIA Insurance Corporation and do not confer rights on third parties; however, these arrangements, together with the ownership of MBIA by MBIA Insurance Corporation and the underwriting support supplied to MBIA by MBIA Insurance Corporation, may make information about MBIA Insurance Corporation of interest to holders of policies and guarantees issued by MBIA. Additionally, the MBIA Assurance Agreements were relevant to the rating agencies in justification of the triple-A ratings granted to MBIA. Any modifications to the Net Worth Maintenance Agreement may not occur without confirmation from each of Standard & Poor's and Moody's that such modifications will not result in the reduction or withdrawal of the claims-paying ratings then assigned to MBIA.

Pursuant to procedures initially developed by MBIA Insurance Corporation, MBIA is selective in the risks which it chooses to underwrite. Logistic and underwriting support are supplied to MBIA from MBIA Insurance Corporation. Logistic review by an analyst of a credit (as hereinafter referred to) and the proposed structure, both the credit and the structure are presented to a separate underwriting committee composed of persons not involved in the analysis. Only following approval of both may a policy or guarantee be issued by MBIA.

Risk Diversification

MBIA guarantees to the holder of the underlying obligation the scheduled payment of the principal of and interest on such obligation. Accordingly, in the case of a default on an insured obligation, payments under the insurance policy cannot be accelerated by the holder. MBIA will be required to pay principal and interest only as originally scheduled payments come due.

MBIA Insurance Corporation and MBIA seek to maintain a diversified insured portfolio designed to spread risk based on a variety of criteria, including revenue source, issue size, type of bond and geographic area. As at 31 December 2000, MBIA Insurance Corporation had 35,154 policies outstanding. These policies are diversified among 10,105 "credits", which MBIA Insurance Corporation defines as any group of issues supported by the same revenue source. MBIA seeks similar diversification. The breakdown of risks insured by MBIA (before reinsurance) and in force as at 31 December 2000 is presented in the following table (*source: audited accounts of MBIA for financial year ended 31 December 2000*):

Table of Risks

	2000	**1999**	**1998**
	(thousands of French Francs)		
Sovereign Risks and Local Authorities	8,663,158	7,825,779	7,805,021
Public Utilities	7,359,797	5,576,120	1,646,953
Structured Financing	7,729,952	8,606,135	12,128,807
Financial Institutions[4]	1,647,671	2,100,140	2,013,678
Investor Owned Utilities	1,676,271	1,048,458	
Total	27,076,849	25,156,632	23,594,459

4 Consists in large part of risks involving smaller banks and insurance companies.

Claims Paying Ability Ratings

Moody's rates the financial strength of each of MBIA Insurance Corporation and MBIA "Aaa".

Standard & Poor's rates the financial strength of each of MBIA Insurance Corporation and MBIA "AAA".

Fitch rates the financial strength of each of MBIA Insurance Corporation and MBIA "AAA".

Each rating of MBIA Insurance Corporation and MBIA should be evaluated independently. The ratings reflect the respective rating agency's current assessment of the creditworthiness of MBIA Insurance Corporation and MBIA and their ability to pay claims on their policies of insurance. Any further explanation as to the significance of the above ratings may be obtained only from the applicable rating agency.

The above ratings are not recommendations to buy, sell or hold the Class A Bonds, and such ratings may be subject to revision or withdrawal at any time by the rating agencies. Any downward revision or withdrawal of any of the above ratings may have an adverse effect on the market price of the Class A Bonds. MBIA Insurance Corporation and MBIA do not guarantee the market price of the Bonds nor do they guarantee that the ratings on the Class A Bonds will not be revised or withdrawn.

Management

As of the date hereof, the members of the Board of Directors of MBIA, their ages and positions within MBIA and their other principal activities are as follows:

Name	Age	Title	Other Activities
John B. Caouette	56	Member of the Board of Directors	Vice Chairman of MBIA Insurance Corporation
Gary C. Dunton	45	Member of the Board of Directors	President and Chief Operating Officer of MBIA Insurance Corporation
Cynthia J. Swift	35	Member of the Board of Directors	Vice President of MBIA Insurance Corporation
Richard L. Weill	58	Member of the Board of Directors	Vice Chairman of MBIA Insurance Corporation
Ram D. Wertheim	46	Member of the Board of Directors	General Counsel of MBIA Inc.
Deborah M. Zurkow	43	President of the Board of Directors	Director of MBIA Insurance Corporation

The board members do not perform any activities which are significant in the context of the issue of the Bonds save as indicated above.

The business address of Ms. Zurkow is 112, avenue Kléber, 75116 Paris, France. The business address of Mr. Caouette is 1 Great St. Helen's, London EC3A 6HX. The business address of Ms Swift and of Messrs Dunton, Weill and Wertheim is 113 King Street, Armonk, New York 10504, United States.

MBIA INSURANCE CORPORATION

General

MBIA Inc. (''**MBIA Inc.**'') is engaged in providing financial guarantee insurance and investment management and financial services to public finance clients and financial institutions on a global basis. Financial guarantees for municipal bonds, asset-backed and mortgage-backed securities, investor-owned utility bonds, and collateralized obligations of sovereigns, corporations and financial institutions, both in the new issue and secondary markets, are provided through MBIA Inc.'s wholly-owned subsidiary, MBIA Insurance Corporation (''**MBIA Insurance Corporation**''). MBIA Insurance Corporation is the successor to the business of the Municipal Bond Insurance Association (the ''**Association**'') which began writing financial guarantees for municipal bonds in 1974. MBIA Insurance Corporation is the parent of MBIA Insurance Corporation of Illinois (''**MBIA Illinois**'') and Capital Markets Assurance Corporation (''**CapMAC**''), both financial guarantee companies. In 1990, MBIA Inc. formed a French insurance company, MBIA, to write financial guarantee insurance in the countries of the European communities. MBIA is 99.99 per cent. owned by MBIA Insurance Corporation, writes policies insuring sovereign risk, public infrastructure financings, asset-backed transactions and certain collateralized obligations of corporations and financial institutions. MBIA has used the provisions of the Insurance Directive to operate in the United Kingdom both on a services and a branch basis. Generally, throughout the text, references to MBIA Insurance Corporation include the activities of its subsidiaries, MBIA Illinois, MBIA and CapMAC. In September 1995, MBIA Insurance Corporation entered into a joint venture agreement with Ambac Assurance Corporation for the purpose of jointly marketing financial guarantee insurance outside the United States. On March 21, 2000, the two companies restructured the joint venture. Under the restructuring, the companies agreed to begin marketing and originating financial guarantee insurance outside the United States independently, and also to continue to maintain certain reciprocal reinsurance arrangements for international business until the end of 2001. MBIA Inc. believes that the restructuring of the joint venture with Ambac will not result in any reduction in premiums written from international business, although no assurances can be given that such a reduction will not occur.

Business and Financial Structure

Financial guarantee insurance provides an unconditional and irrevocable guarantee of the payment of the principal of, and interest or other amounts owing on, insured obligations when due. MBIA Insurance Corporation primarily insures obligations which are sold in the new issue and secondary markets, or which are held in unit investment trusts (''**UIT**'') and by mutual funds. It also provides surety bonds for debt service reserve funds. The principal economic value of financial guarantee insurance to the entity offering the obligations is the savings in interest costs resulting from the difference in the market yield between an insured obligation and the same obligation on an uninsured basis. In addition, for complex financings and for obligations of issuers that are not well-known by investors, insured obligations receive greater market acceptance than uninsured obligations. The municipal obligations that MBIA Insurance Corporation insures include tax-exempt and taxable indebtedness of states, counties, cities, utility districts and other political subdivisions, as well as airports, higher education and health care facilities and similar authorities. The asset-backed or structured finance obligations insured by MBIA Insurance Corporation typically consist of securities that are payable from or which are tied to the performance of a specified pool of assets that have a defined cash flow. These include residential and commercial mortgages, a variety of consumer loans, corporate loans and bonds and equipment and real property leases. The transactions insured by the joint venture include sovereign and sub-sovereign debt, as well as structured finance transactions.

MBIA Insurance Corporation has a Triple-A claims-paying rating from Standard and Poor's, which it received in 1974; from Moody's, which it received in 1984; from Fitch, which it received in 1995; and from Japan Rating and Investment Information, Inc. (''**JRII**''), which it received in 1998. Obligations which are guaranteed by MBIA Insurance Corporation are rated Triple-A primarily based on these claims-paying ratings of MBIA Insurance Corporation. Both Standard & Poor's and Moody's have also continued the Triple-A rating on MBIA Illinois and CapMAC guaranteed bond issues. The Triple-A ratings are important to the operation of MBIA Inc.'s business and any reduction in these ratings could have a material adverse effect on MBIA Insurance Corporation's ability to compete and could have a material adverse effect on the business, operations and financial results of MBIA Inc.

MBIA Inc. also provides investment management products and financial services through a group of subsidiary companies. These services include cash management, municipal investment agreements, discretionary asset management, purchase and administrative services, and municipal

revenue enhancement services. MBIA Municipal Investors Service Corporation ("**MBIA-MISC**") provides cash management services and investment placement services to local governments and school districts, and provides those clients with fund administration services. American Money Management Associates, Inc. ("**AMMA**") offers investment and treasury management consulting services to municipal and quasi-municipal clients. MBIA Investment Management Corp. ("**IMC**") offers guaranteed investment agreements primarily for bond proceeds to states and municipalities. MBIA Capital Management Corp. ("**CMC**") performs investment management services for MBIA Insurance Corporation, MBIA-MISC, IMC and selected external clients. In 1998, the company acquired 1838 Investment Advisors, Inc. ("**1838**"), a provider of asset management services. In 1999, MBIA Inc. formed a holding company, MBIA Asset Management Corporation, to consolidate the resources and capabilities of these four entities.

Capitalisation and Indebtedness Table

The following table sets forth the capitalisation and indebtedness of MBIA Insurance Corporation as at 31 December 2000 and 31 December 1999 (*source: audited accounts of MBIA Insurance Corporation for financial year ended 31 December 2000*):

	31 December 2000	**31 December 1999**
	(US$ in thousands) (audited)	
Long-term Debt	Nil	Nil
Investors Equity:		
Common stock, par value $150 per share; authorised, issued and outstanding – 100,000 shares	15,000	15,000
Additional paid-in capital[1]	1,540,071	1,514,014
Retained earnings	3,191,536	2,858,210
Accumulated other comprehensive income	60,999	159,597
Total Investors' Equity	US$ 4,807,606	US$ 4,227,627
Total Capitalisation and Indebtedness[2]	US$ 4,807,606	US$ 4,227,627

1 Represents the additional contribution from MBIA Inc. above the par value of the common stock.

2 There has been no material change in the capitalisation and indebtedness of MBIA Insurance Corporation since the date of this Capitalisation and Indebtedness Table, and MBIA Insurance Corporation has no material contingent liabilities or guarantees.

Risk Diversification

At 31 December 2000, the net par amount outstanding on MBIA Insurance Corporation's insured obligations (including insured obligations of MBIA Illinois, MBIA and CapMAC) was US$418.4 billion, comprised of US$349.8 billion in new issues and US$68.6 billion in secondary market issues. Net insurance in force was US$680.9 billion (excluding US$5.3 billion relating to municipal investment agreements of IMC guaranteed by MBIA Insurance Corporation).

MBIA Insurance Corporation seeks to maintain a diversified insured portfolio designed to spread risk based on a variety of criteria, including revenue source, issue size, type of bond and geographic area. As of 31 December 2000, MBIA Insurance Corporation has 35,154 policies outstanding. These policies are diversified among 10,105 "credits", which MBIA Insurance Corporation defines as any group of issues supported by the same revenue source.

MBIA Insurance Corporation underwrites financial guarantee insurance on the assumption that the insurance will remain in force until maturity of the insured obligations. MBIA Insurance Corporation estimates that the average life (as opposed to the stated maturity) of its insurance policies in force at 31 December 2000 was 11.0 years. The average life was determined by applying a weighted average calculation, using the remaining years to maturity of each insured obligation, and weighing them on the basis of the remaining debt service insured. No assumptions were made for any future refundings of insured issues. Average annual debt service on the portfolio at 31 December 2000 was US$51.7 billion.

Reinsurance

State insurance laws and regulations, as well as Moody's and Standard & Poor's, impose minimum capital requirements on financial guarantee companies, limiting the aggregate amount of insurance which may be written and the maximum size of any single risk exposure which may be assumed. MBIA Insurance Corporation increases its capacity to write new business by using treaty and facultative reinsurance to reduce its gross liabilities on an aggregate and single risk basis.

As a primary insurer, MBIA Insurance Corporation is required to honour its obligations to its policyholders whether or not its reinsurers perform their obligations to MBIA Insurance Corporation. The financial position of all reinsurers is monitored by MBIA Insurance Corporation on a regular basis.

Regulation

MBIA Insurance Corporation is licensed to do insurance business in, and is subject to insurance regulation and supervision by, the State of New York (its state of incorporation), the 49 other US states, the District of Columbia, Guam, the Northern Mariana Islands, the U.S. Virgin Islands, Puerto Rico, the Kingdom of Spain and the French Republic. MBIA is licensed to do insurance business in the French Republic and is subject to regulations under the corporation and insurance laws of the French Republic. MBIA has used the provisions of the Insurance Directive to operate in the United Kingdom both on a services and a branch basis and is to a limited extent subject to supervision by the Financial Services Authority. The extent of state insurance regulation and supervision varies by jurisdiction, but New York, Illinois and most other jurisdictions have laws and regulations prescribing minimum standards of solvency, including minimum capital requirements and business conduct which must be maintained by insurance companies. These laws prescribe permitted classes and concentrations of investments. In addition, some state laws and regulations require the approval or filing of policy forms and rates. MBIA Insurance Corporation is required to file detailed annual financial statements with the New York Insurance Department and similar supervisory agencies in each of the other jurisdictions in which it is licensed. The operations and accounts of MBIA Insurance Corporation are subject to examination by these regulatory agencies at regular intervals. MBIA Inc. is subject to the direct and indirect effects of governmental regulation, including changes in tax laws affecting the municipals and asset-backed debt markets. No assurance can be given that future legislative or regulatory changes might not adversely affect the results of operations and financial conditions of MBIA Inc.

MBIA Insurance Corporation is licensed to provide financial guarantee insurance under Article 69 of the New York Insurance Law. Article 69 defines financial guarantee insurance to include any guarantee under which loss is payable upon proof of occurrence of financial loss to an insured as a result of certain events. These events include the failure of any obligor on or any issuer of any debt instrument or other monetary obligation to pay principal, interest, premium, dividend or purchase price of or on such instrument or obligation, when due. Under Article 69, MBIA Insurance Corporation is licensed to transact financial guarantee insurance, surety insurance and credit insurance and such other kinds of business to the extent necessarily or properly incidental to the kinds of insurance which MBIA Insurance Corporation is authorised to transact. In addition, MBIA Insurance Corporation is empowered to assume or reinsure the kinds of insurance described above.

As a financial guarantee insurer, MBIA Insurance Corporation is required by the laws of New York, California, Connecticut, Florida, Illinois, Iowa, New Jersey and Wisconsin to maintain contingency reserves on its municipal bond and other financial guarantee liabilities. Under New Jersey, Illinois and Wisconsin regulations, contributions by such an insurer to its contingency reserves are required to equal 50 per cent. of earned premiums on its municipal bond business. Under New York law, such an insurer is required to contribute to contingency reserves 50 per cent. of premiums as they are earned on policies written prior to 1 July 1989 (net of reinsurance) and, with respect to policies written on and after 1 July 1989, must make contributions over a period of 15 or 20 years (based on issue type), or until the contingency reserve for such insured issues equals the greater of 50 per cent. of premiums written for the relevant category of insurance or a percentage of the principal guaranteed, varying from 0.55 per cent. to 2.5 per cent., depending upon the type of obligation guaranteed (net of reinsurance, refunding, refinancings and certain insured securities). California, Connecticut, Iowa and Florida law impose a generally similar requirement. In each of these states, MBIA Insurance Corporation may apply for release of portions of the contingency reserves in certain circumstances.

The laws and regulations of these states also limit both the aggregate and individual municipal bond risks that MBIA Insurance Corporation may insure on a net basis. California, Connecticut, Florida, Illinois and New York, among other things, limit insured average annual debt services on insured

municipal bonds with respect to a single entity and backed by a single revenue source (net of qualifying collateral and reinsurance) to 10 per cent. of policyholders' surplus and contingency reserves. In New Jersey, Virginia and Wisconsin, the average annual debt service on any single issue of municipal bonds (net of reinsurance) is limited to 10 per cent. of policyholders' surplus. Other states that do not explicitly regulate financial guarantee or municipal bond insurance do impose single risk limits which are similar in effect to the foregoing. California, Connecticut, Florida, Illinois and New York also limit the net insured unpaid principal issued by a single entity and backed by a single revenue source to 75 per cent. of policyholders' surplus and contingency reserves.

Under New York, California, Connecticut, Florida, Illinois, New Jersey and Wisconsin law, aggregate insured unpaid principal and interest under policies insuring municipal bonds (in the case of New York, Connecticut, Florida and Illinois, net of reinsurance) are limited to certain multiples of policyholders' surplus and contingency reserves. New York, California, Connecticut, Florida, Illinois and other states impose a 300:1 limit for insured municipal bonds, although more restrictive limits on bonds of other types do exist. For example, New York, California and Florida impose a 100:1 limit for certain types of non-municipal bonds.

MBIA Inc., MBIA Insurance Corporation, MBIA Illinois and CapMAC are subject to regulation under the insurance holding company statutes of New York, Illinois and other jurisdictions in which MBIA Insurance Corporation, MBIA Illinois and CapMAC are licensed to write insurance. The requirements of holding company statutes vary from jurisdiction to jurisdiction but generally require insurance holding companies, such as MBIA Inc., and their insurance subsidiaries, to register and file certain reports describing, among other information, their capital structure, ownership and financial condition. The holding company statutes also require prior approval of changes in control, of certain dividends and other intercorporate transfers of assets, and of transactions between insurance companies, their parents and affiliates. The holding company statutes impose standards on certain transactions with related companies, which include, among other requirements, that all transactions be fair and reasonable and that those exceeding specified limits receive prior regulatory approval.

Prior approval by the New York Insurance Department is required for any entity seeking to acquire "control" of MBIA Inc., MBIA Insurance Corporation, or CapMAC. Prior approval by the Illinois Department of Insurance is required for any entity seeking to acquire "control" of MBIA Inc., MBIA Insurance Corporation or MBIA Illinois. In many states, including New York and Illinois, "control" is presumed to exist if 10 per cent. or more of the voting securities of the insurer are owned or controlled by an entity, although the supervisory agency may find that "control" in fact does or does not exist when an entity owns or controls either a lesser or greater amount of securities.

The laws of New York and Illinois regulate the payment of dividends by MBIA Insurance Corporation and provide that a New York domestic stock property/casualty insurance company (such as MBIA Insurance Corporation) may not declare or distribute dividends except out of statutory earned surplus. New York law provides that the sum of (i) the amount of dividends declared or distributed during the preceding 12-month period and (ii) the dividend to be declared may not exceed the lesser of (a) 10 per cent. of policyholders' surplus, as shown by the most recent statutory financial statement on file with the New York Insurance Department, and (b) 100 per cent. of adjusted net investment income for such 12-month period (the net investment income for such 12-month period plus the excess, if any, of net investment income over dividends declared or distributed during the two-year period preceding such 12-month period), unless the New York Superintendent of Insurance approves a greater dividend distribution based upon a finding that the insurer will retain sufficient surplus to support its obligations and writings. See Note 15 to the Consolidated Financial Statements of MBIA Inc. and Subsidiaries.

The foregoing dividend limitations are determined in accordance with Statutory Accounting Practices ("**SAP**"), which generally produce statutory earnings in amounts less than earnings computed in accordance with Generally Accepted Accounting Principles ("**GAAP**"). Similarly, policyholders' surplus, computed on a SAP basis, will normally be less than net worth computed on a GAAP basis. See Note 7 to the Consolidated Financial Statements of MBIA Inc. and Subsidiaries.

MBIA Insurance Corporation, MBIA Illinois and CapMAC are exempt from assessments by the insurance guarantee funds in the majority of the states in which they do business. Guarantee fund laws in most states require insurers transacting business in the state to participate in guarantee associations which pay claims of policyholders and third-party claimants against impaired or insolvent insurance

companies doing business in the state. In most cases, insurers licensed to write only municipal bond insurance, financial guarantee insurance and other forms of surety insurance are exempt from assessment by these funds and their policyholders are prohibited from making claims on these funds.

Management

At 31 December 2000, the executive officers and their present ages and positions within MBIA Insurance Corporation are set forth below:

Name	Age	Position
Joseph W. Brown	51	Chairman and Chief Executive Officer
Gary C. Dunton	45	President and Chief Operating Officer
Richard L. Weill	58	Vice Chairman and Secretary
John B. Caouette	56	Vice Chairman
Neil G. Budnick	46	Vice Chairman and Chief Financial Officer
Ram D. Wertheim	46	General Counsel

Recent Developments[8]

For the year ended 31 December 2000, MBIA Insurance Corporation had net income of US$530.6 million as compared to US$472.0 million the year ended 31 December 1999. At 31 December 2000, MBIA Insurance Corporation's investor's equity was US$4.8 billion.

MBIA Insurance Corporation guaranteed US$98.8 billion of par value in the year 2000, an increase of 7.3 per cent. over the US$92.1 billion of par insured in the same 1999 period. In the year 2000, MBIA Insurance Corporation insured US$32.8 billion of par value of municipal bonds, an 8.4 per cent. decrease from US$35.8 billion insured in the same 1999 period. In the domestic structured finance market, which includes mortgage-backed and asset-backed transactions, MBIA Insurance Corporation insured US$47.9 billion of par value, an increase of 4.4 per cent. from the US$45.9 billion insured in the same period last year. In addition, MBIA Insurance Corporation insured US$18.6 billion of securities internationally compared with US$7.6 billion in 1999.

Gross premiums written for the year 2000 increased to US$687.4 million from US$624.9 million a year ago. Premiums earned in the year 2000 were US$446.4 million, up from US$442.8 million in the comparable 1999 period. Net investment income, excluding net realised capital gains, increased in 2000 to US$392.1 million from US$358.8 million in 1999. Revenues of MBIA Insurance Corporation in year ended 31 December 2000 increased to US$888.7 million compared with US$857.2 million for the year ended 31 December 2000. Total expenses for the year ended 31 December 2000 were US$167.6 million compared to US$311.8 million for the year ended 31 December 1999.

Computed on a statutory basis, as of 31 December 2000, MBIA Insurance Corporation's unearned premium reserve was US$2.5 billion, and its capital base, consisting of capital and surplus and contingency reserve, was US$4.5 billion. Aggregate policyholders' reserves at 31 December 2000, rose to US$7.2 billion, compared with US$6.7 billion at 31 December 1999.

8 The source of the financial information appearing in the section entitled "Recent Developments" is MBIA Insurance Corporation's books and records.

MBIA BOND POLICY

Each MBIA Bond Policy and its endorsement (to which the relevant MBIA Bond Policy is subject and which modifies some of its provisions) will be substantially in the form of the following, subject to completion and immaterial amendment.

MBIA Assurance S.A.
London Branch
1 Great St. Helen's
2nd Floor
London EC3A 6HX
United Kingdom

Telephone: 00 44 20 7920 6363
Fax: 00 44 7588 3393

Financial Guarantee Insurance Policy in respect of Class A Bonds

Policy Number: [●]

Insured Obligations: the payment obligations of Dwr Cymru (Financing) Limited (the "**Issuer**") in respect of each amount of Principal and Interest owing by the Issuer and outstanding pursuant to the Issuer's Guaranteed Asset-Backed Sub-Class A-[●] Bonds due [●] (the "**Class A Bonds**")

Beneficiary: Bankers Trustee Company Limited or any additional or successor trustee appointed pursuant to the Trust Deed as trustee for the Holders of the Insured Obligations (the "**Bond Trustee**")

MBIA Assurance S.A. ("**MBIA**"), a *société anonyme* incorporated under the laws of the French Republic (registered with the Paris Register of Trade and Companies under No. B377883293 (98 B 05130)) and acting through its registered branch office in England and Wales (registration number BR003789) in consideration of the payment of the premium and subject to the terms of the Policy (including the endorsement attached hereto), hereby agrees unconditionally and irrevocably to pay to the Bond Trustee for the benefit of the Holders of the Insured Obligations an amount equal to that portion of the Insured Amounts which shall become Due for Payment but shall have remained unpaid by reason of Nonpayment.

MBIA will make any such payments to the Bond Trustee from its own funds by 11.00 am on the later of (a) the day which is four (4) Business Days following notification to MBIA of Nonpayment or (b) the day on which the Insured Amounts are Due for Payment or, if that is not a Business Day, on the next succeeding Business Day. Such payments of Principal or Interest shall be made only upon presentation to MBIA of (i) a validly completed Notice of Claim signed by the Bond Trustee and in the form hereto attached; and (ii) an instrument of assignment in form and substance satisfactory to MBIA, transferring to MBIA all rights under such Insured Obligations, including the right to receive Principal and Interest in respect of the Insured Obligations free of any adverse claim. MBIA shall be subrogated to the Holders' rights to payment on the Insured Obligations to the extent of any payments made by MBIA under the Policy. Once payments of any Insured Amounts have been made to the Bond Trustee or as the Bond Trustee shall have directed, MBIA shall have no further obligation hereunder in respect of such Insured Amounts.

In the event that the Bond Trustee has notice that any payment of Insured Amounts in respect of the Insured Obligations which has become Due for Payment and which was made to the Bond Trustee or a Holder by or on behalf of the Issuer has been deemed an unfair preference and recovered from the Bond Trustee or such Holder pursuant to sections 239 to 244 of the Insolvency Act 1986 or otherwise pursuant to applicable bankruptcy or insolvency law in accordance with a final, non-appealable order of a court of competent jurisdiction, the Bond Trustee or such Holder will be entitled to payment from MBIA to the extent of such recovery if sufficient funds are not otherwise available.

The Policy is non-cancellable by MBIA for any reason, including failure by MBIA to receive payment of any premium due hereunder. The premium on the Policy is not refundable by MBIA for any reason. The Policy does not insure against loss of any prepayment or other acceleration payment which

at any time may become due in respect of any Insured Obligation, other than at the sole option of MBIA as specified below, nor against any risk other than Nonpayment, including failure of the Bond Trustee or any Paying Agent to make any payment due to Holders of Insured Amounts.

To the fullest extent permitted by applicable law, MBIA hereby waives for the benefit of the Bond Trustee and each Holder and agrees not to assert any and all rights (whether by counterclaim, set-off or otherwise) and defences (including, without limitation, any defence of fraud or any defence based on non-disclosure of information by any person) whether acquired by subrogation, assignment or otherwise to the extent such rights and defence may be available to MBIA to avoid payment of its obligations under the Policy in accordance with the express provisions of the Policy.

All payments of Insured Amounts by MBIA shall be made without withholding or deduction for, or on account of, any present or future tax, duties, assessment or other governmental charges of whatever nature, unless the withholding or deduction of such tax, assessment or other governmental charge is required by law or regulation or administrative practice of any jurisdiction. If any such withholding or deduction is required, MBIA shall pay the Insured Amounts net of such withholding or deduction and shall account to the appropriate tax authority for the amount required to be withheld or deducted. **MBIA shall not be obliged to pay any amount to the Bond Trustee or any Holder in respect of the amount of such withholding or deduction.**

Any capitalised terms not defined herein shall have the meaning given to such terms in the endorsement attached hereto, which forms an integral part of the Policy.

Unless prior to such date the Issuer has become subject to any insolvency or analogous proceedings in respect of its insolvency, winding up or administration under any applicable Insolvency Law, the Policy shall terminate on the date falling two years and one day after the last Payment Date and MBIA shall cease upon such date to be liable for any claim made in respect hereof after such date.

The Policy shall be governed by and construed in accordance with the laws of England and Wales.

IN WITNESS WHEREOF MBIA has caused the Policy to be signed by its duly authorised representative.

MBIA ASSURANCE S.A.

Authorised Representative

Effective Date:

MBIA Assurance S.A.
London Branch
1, Great St. Helen's
2nd Floor
London EC3A 6HX
United Kingdom

Telephone: 00 44 20 7920 6363
Fax: 00 44 20 7588 3393

Financial Guarantee Insurance Policy Endorsement (the "Endorsement")

Effective Date of Endorsement: [●]

Attached to and forming a part of Policy No. [●] (the "**Policy**") issued in respect of:

Insured Obligations: the payment obligations of the Issuer in respect of each amount of Principal and Interest owing by the Issuer and outstanding pursuant to the Issuer's Guaranteed Asset-Backed Sub-Class A-[●] Bonds due [●] (the "**Class A Bonds**").

For all purposes of the Policy, the following terms shall have the following meanings:

"**Affiliate**" shall mean, as to any person which directly or indirectly through one or more intermediaries controls, or is controlled by, or is under common control with, the first person where "**control**" means the possession, directly or indirectly of the power to direct or cause the direction of the management or policies of a person, whether through the ownership of voting stock, by contract or otherwise.

"**Bond Trustee**" shall mean Bankers Trustee Company Limited or any additional or successor trustee appointed pursuant to the terms of the Trust Deed, which expression includes any modification or supplement thereto.

"**Business Day**" shall have the same meaning as given to it pursuant to Condition 6(i) of the Conditions.

"**Conditions**" shall mean the terms and conditions of the Class A Bonds as may from time to time be amended, varied or supplemented.

"**DCC**" means Dŵr Cymru Cyfyngedig.

"**Due for Payment**" shall mean due and payable on a Payment Date.

"**Holder**" shall mean the holder or holders of one or more Class A Bonds, being the holder(s) of Insured Obligations.

"**Insurance and Indemnity Agreement**" shall mean the agreement dated on or around the date of this Policy, governed by the laws of England and Wales, between the Issuer, DCC and MBIA pursuant to which, *inter alia*, MBIA has agreed to issue the Policy subject to the satisfaction (or waiver by MBIA) of certain conditions precedent, in particular the payment to MBIA of the premium, and the Issuer has agreed, *inter alia*, to indemnify MBIA for, and to MBIA being subrograted to the rights of the Holders in respect of any payments made by MBIA under the Policy.

"**Insured Amounts**" shall mean, with respect to any Payment Date, the sum of (i) an amount equal to the amount of Interest due on the Insured Obligations as of such Payment Date and (ii) an amount equal to the Principal due on the Insured Obligations on such Payment Date.

"**Insured Obligations**" shall mean the payment obligations of the Issuer in respect of each amount of Principal and Interest owing by the Issuer and outstanding and Due for Payment under the Class A Bonds.

"**Interest**" shall mean any amount in respect of regularly scheduled interest (as adjusted for indexation in accordance wih the Conditions, if applicable) owing by the Issuer under the Class A Bonds when issued excluding any amount relating to prepayment, early redemption, broken funding indemnities, penalties or default interest.

"**Issuer**" shall mean Dwr Cymru (Financing) Limited a company incorporated as an exempt company in the Cayman Islands with registered number 108127.

"**Issuer Transaction Documents**" shall have the meaning given to it pursuant to the Conditions.

"**Nonpayment**" shall mean, as of any Payment Date, the failure by the Issuer to pay all or any part of any Insured Amount.

"**Notice of Claim**" shall mean the notice of claim and certificate attached hereto.

"**Paying Agency Agreement**" shall have the meaning given to it pursuant to the Conditions.

"**Payment Date**" shall mean:

(a) in respect of Interest, an Interest Payment Date (as defined in Condition 6(i));

(b) in respect of Principal, the scheduled dates for repayment specified in the Conditions; and

(c) any earlier date for the payment of Interest or repayment of Principal to which MBIA shall have consented at its sole discretion.

"**Principal**" shall mean the Principal Amount Outstanding (as defined in Condition 6(i) and as adjusted for indexation in accordance with the Conditions if applicable), excluding (if MBIA elects in its sole discretion to accelerate payments due under the Policy) any additional amount relating to prepayment, early redemption, broken funding indemnities or penalties.

"**Principal Paying Agent**" shall have the meaning given to it pursuant to the Conditions.

"**Receipt**" shall mean actual delivery of the Notice of Claim to MBIA at its address above (or such other office as shall have been notified by MBIA to the Bond Trustee from time to time by at least seven Business Days' notice) prior to 12.00 noon, London time, on a Business Day. Delivery either on a day that is not a Business Day or after 12.00 noon, London time shall be deemed to be received on the next succeeding Business Day.

The Policy is hereby amended to provide that:

(i) There shall be no acceleration payment due under the Policy unless any such acceleration is, at the sole option of MBIA, communicated in writing by MBIA to the Bond Trustee without the need for Receipt of a Notice of Claim. In the event that MBIA decides in its absolute discretion to accelerate any payments due under the Policy, nothing in the Policy shall oblige MBIA to make payments in respect of any part of the Insured Obligations which would be greater than the outstanding principal amount of such part of the Insured Obligations (plus accrued but unpaid interest and amounts in respect of indexation, if applicable) and MBIA's obligations under the Policy shall be satisfied in full by the payment of such outstanding amount in accordance with the terms of the Policy. MBIA may elect to accelerate payments due under the Policy in full or partially.

(ii) All notices including the Notice of Claim shall be delivered by registered mail or personally delivered to MBIA at the address set out in the Notice of Claim or such other different address or addresses as MBIA may notify in writing to the Bond Trustee. If any Notice of Claim given hereunder by the Bond Trustee is not in proper form or is not properly completed, executed or delivered, it shall be deemed not to have been received and MBIA shall promptly so advise the Bond Trustee and the Bond Trustee may submit to MBIA an amended Notice of Claim.

(iii) MBIA hereby agrees that the Trust Deed shall be treated as if it were an instrument of assignment in form and substance satisfactory to it for the purposes of the Policy and acknowledges that the Trust Deed has been presented to it by the Bond Trustee as required by the Policy.

(iv) At any time during the term of the Policy, MBIA may appoint a fiscal agent ("the **Fiscal Agent**") for the purposes of the Policy by written notice to the Bond Trustee at the notice address specified in the Trust Deed specifying the name and notice address of the Fiscal Agent, which Fiscal Agent shall be situated in the City of New York or London. From and after the date of receipt of such notice by the Bond Trustee, (i) copies of all notices including the Notice of Claim and other documents required to be delivered to MBIA pursuant to the Policy shall be simultaneously delivered to the Fiscal Agent and to MBIA and shall not be deemed to be received until it is received by both the Fiscal Agent and MBIA, and (ii) all payments required to be made by MBIA under the Policy shall be made directly by MBIA or by the Fiscal Agent on behalf of MBIA, provided, however, that payment by MBIA to any Fiscal Agent shall not discharge MBIA's obligations hereunder in respect of Scheduled Payments. The Fiscal Agent is the agent of MBIA only and the Fiscal Agent shall in no event

be liable to the Bond Trustee nor to any Holder for any acts of the Fiscal Agent or any failure of MBIA to deposit, or cause to be deposited, sufficient funds to make payments under the Policy.

"**Trust Deed**" shall have the meaning given to it in the Conditions.

In the event that any term or provision on the face of the Policy is inconsistent with the provision of this Endorsement, the provisions of this Endorsement shall take precedence and shall be binding.

The obligations of MBIA hereunder may be assigned or transferred by MBIA to any Affiliate of MBIA provided that, *inter alia*:

(i) no MBIA Event of Default (as defined in the Master Framework Agreement) has occurred and is continuing at the time of such assignment or transfer;

(ii) MBIA or such assignee or transferee delivers to the Bond Trustee written confirmation from any two of the Rating Agencies (as defined in the Master Framework Agreement) that, at the time of such assignment or transfer, the claims paying ability of such Affiliate was rated at least equal to the claims paying ability of MBIA at that time; and

(iii) MBIA or such assignee or transferee thereafter delivers to the Bond Trustee written notice of any such assignment or transfer and such assignee or transferee accedes to the relevant Issuer Transaction Documents.

The Policy shall be governed by and construed in accordance with the laws of England and Wales.

MBIA irrevocably waives any objection which it might now or hereafter have to the courts of England and Wales being nominated as the forum to hear and determine any suit, action or proceedings, and to settle any disputes, which arises out of or in connection with the Policy, and agrees not to claim that any such court is not a convenient or appropriate forum.

The obligations of MBIA under the Policy shall not be affected by any redenomination of the Insured Obligations into euro pursuant to Condition 19 save that, following any such redenomination, payments of Insured Amounts hereunder shall be made in euro.

Nothing herein contained shall be held to vary, alter, waive or extend any of the terms, conditions, provisions, agreements or limitations of the Policy other than as above stated.

Any right under the UK Contract (Rights of Third Parties) Act 1999 which any person (other than MBIA as issuer of the Policy and the Bond Trustee as beneficiary of the Policy) may otherwise have to enforce any term or condition of the Policy and this Endorsement is expressly excluded.

Unless prior to such date the Issuer has become subject to any insolvency or analogous proceedings in respect of its insolvency, winding up or administration under any applicable Insolvency Law, the Policy shall terminate on the date falling two years and one day after the last Payment Date and MBIA shall cease on such date to be liable for any claim made in respect hereof after such date.

IN WITNESS WHEREOF MBIA has caused this Endorsement to the Policy to be signed by its duly authorised representative.

MBIA ASSURANCE S.A.

Authorised Representative
Effective Date:

Notice of Claim

MBIA Assurance S.A.
London Branch
1, Great St. Helen's
2nd Floor
London EC3A 6HX
United Kingdom

Telephone: 00 44 20 7920 6363
Fax: 00 44 20 7588 3393

Attention: The Director

[and the Fiscal Agent as the case may be]

The undersigned, a duly authorised officer of Bankers Trustee Company Limited or any additional or successor trustee appointed pursuant to the terms of the Trust Deed (the "**Bond Trustee**"), hereby certifies to MBIA Assurance S.A. ("**MBIA**"), with reference to Financial Guarantee Insurance Policy No. [●] and the endorsement thereto dated [*insert date*] (together, the "**Policy**") issued by MBIA in respect of the payment obligations of Dwr Cymru (Financing) Limited (the "**Issuer**") in respect of each amount of Principal and Interest owing by the Issuer and outstanding pursuant to the Issuer's Guaranteed Asset-Backed Sub-Class A-[●] Bonds (the "**Insured Obligations**"), that:

(i) The Bond Trustee is the trustee for Holders under the Trust Deed;

(ii) The Bond Trustee has been notified by the Principal Paying Agent that the deficiency in respect of Insured Amounts which are Due for Payment on *[insert Payment Date]* will be £/€/$ *[insert applicable amount]* (the "**Shortfall**");

(iii) The Bond Trustee is making a claim under the Policy for the Shortfall to be applied to the payment of Insured Amounts which are Due for Payment.

(iv) The Bond Trustee agrees that, following payment of funds by MBIA, it shall procure that (a) it shall hold such amounts in trust and procure that such amounts are applied directly to the payment of Insured Amounts which are Due for Payment; (b) such funds are not applied for any other purpose; (c) such funds are not commingled with other funds held by the Bond Trustee; and (d) a record of such payments with respect to each Insured Obligation and the corresponding claim on the Policy and the proceeds thereof is maintained by the Principal Paying Agent in accordance with the terms of the Paying Agency Agreement; and

(v) The Bond Trustee acknowledges that under the Trust Deed it has assigned to MBIA its rights to receive any payments from the Issuer in respect of the Insured Obligations to the extent of any payments which have been made under the Policy. The foregoing assignment is in addition to, and not in limitation of, rights of subrogation otherwise available to MBIA in respect of such payments. The Bond Trustee shall take such action and deliver such instruments as may be reasonably requested or required by MBIA to effectuate the purpose or provisions of this clause (v).

(vi) payment should be made [in £/€/$] by [credit] to a designated [pounds Sterling/euro/United States Dollar account of the *[insert payee]* at *[insert account details]* with *[insert bank details]*;

Unless the context otherwise requires, capitalised terms used in this Notice of Claim and not defined herein shall have the meanings provided in the Policy.

This Notice of Claim may be revoked by written notice by the Bond Trustee to MBIA at any time prior to 10.00 a.m. (London time) on the second Business Day prior to the date specified above on which Insured Amounts are Due for Payment if and only to the extent that moneys are actually received in respect of the Insured Obligations prior to such time from a source other than MBIA.

This Notice of Claim shall be governed by and construed in accordance with the laws of England and Wales.

IN WITNESS WHEREOF the Bond Trustee has executed and delivered this Notice of Claim on the *[insert date]* day of *[insert date].*

Bankers Trustee Company Limited

By:...

Title:..

For MBIA Assurance S.A. or Fiscal Agent Use Only

Wire transfer sent on ________________________ By ___________________

Confirmation Number

CHAPTER 8

WATER REGULATION

WATER REGULATION GENERALLY

Background

The current structure of the water industry in England and Wales dates from 1989, when the UK Water Act 1989 (the "**1989 Act**") was enacted. Before this, there were ten regional public sector water and sewerage authorities (the "**Water Authorities**") supplying water and sewerage services and 29 privately owned statutory water companies, supplying water only. Under the 1989 Act, 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 water and sewerage companies in England and Wales. The industry is now made up of ten water and sewerage companies and seventeen water only companies which are all subject to the same regulatory regime (together, the "**Regulated Companies**" and each a "**Regulated Company**"). The 1989 Act's provisions are now contained in the consolidating UK Water Industry Act 1991 (as amended by subsequent legislation, including the Competition and Service (Utilities) Act 1992 and the Water Industry Act 1999) (the "**WIA**"). References in this section to statutes are to the WIA unless otherwise stated.

Regulatory Framework

The activities of Regulated Companies are principally regulated by the provisions of the WIA, regulations made under the WIA and the conditions of their instruments of appointment as water undertakers and sewerage undertakers (together "**licences**" and each a "**licence**"). 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.

In relation to appointments made in the Dŵr Cymru and Dee Valley areas of appointment, certain of the powers of the Secretary of State have been transferred to the National Assembly for Wales (the "**Assembly**") (see "*The Assembly*" below). Accordingly, references to the Secretary of State will, as the context may require, be deemed to include reference to the Assembly in respect of such powers and responsibilities.

The economic regulator for water is the DGWS who is aided in his duties by Ofwat, a non-ministerial government department, of which he is head. Ofwat is responsible for, *inter alia*, setting limits on charges and monitoring and enforcing licence obligations. 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 affairs. The two principal quality regulators are the Drinking Water Inspectorate (the "**DWI**"), which is part of the Department for the Environment, Transport and Regions (the "**DETR**"), and the Environment Agency (the "**EA**").

The DGWS and the Secretary of State

The DGWS is appointed for a fixed term by the Secretary of State (in consultation with the Assembly). 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. He replaced Sir Ian Byatt, who had been the DGWS for the previous 11 years.

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.

Subject to this primary duty 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 (especially rural customers) in connection with the fixing and recovery of water and drainage charges, and such that no undue preference or discrimination is shown in the fixing of those charges;
- protect the interests of customers in connection with the terms on which services are provided and the quality of those services;
- protect the interest of customers as regards non-regulated activities of Regulated Companies (and companies connected with them) 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 disposal by Regulated Companies of "protected land";
- promote economy and efficiency on the part of Regulated Companies; and
- facilitate effective competition between Regulated Companies and those seeking appointments as Regulated Companies.

The Assembly

The Assembly was established by the Government of Wales Act 1998 (the "**GWA**") which largely defines the make-up, powers and functions of the Assembly. The Assembly's relationship with the UK Government and Whitehall departments is set out in a Memorandum of Understanding. The Assembly develops and implements policies which reflect the particular needs of the people of Wales. The GWA sets out essential structures and procedures for the Assembly and more detailed processes are set out in the Assembly Standing Orders.

Devolved powers and responsibilities under the WIA were transferred from the Secretary of State to the Assembly by the National Assembly for Wales (Transfer of Functions) Order 1999 on 1 July 1999, by the National Assembly for Wales (Transfer of Functions) (No. 2) Order on 15 November 1999 and by the National Assembly for Wales (Transfer of Functions) Order 2000 on 8 February 2000 (together, the "**Wales (Transfer of Functions) Orders**"). Elections for the first Assembly were held on 6 May 1999 and future elections will be held every four years.

The Assembly elects the First Secretary (also known as the "**First Minister**") to whom the sixty members delegate their executive powers. The current First Minister is Rhodri Morgan. The First Minister delegates responsibility for the execution of such executive functions to a number of Assembly Secretaries who form the Assembly's executive committee, the "**Assembly Cabinet**", which is accountable to the rest of the Assembly and makes many of its day to day decisions. Subject Committees develop policies concerning issues such as health, education, economic development and the environment and are made up of elected members of the Assembly. There are also Regional Committees which examine local needs and interests, bringing them to the attention of the Subject Committees and the Assembly as a whole.

Under the Wales (Transfer of Functions) Orders the majority of the functions of the Secretary of State set out in the WIA are transferred, in as far as they relate to Regulated Companies whose areas are wholly or mainly in Wales, to the Assembly.

Those duties, powers and functions transferred include:

- general duties with respect to the water industry;
- the power to appoint (or to consent or give a general authorisation for the DGWS to appoint) a company to be a Regulated Company;
- the duty to secure the appointment of relevant Regulated Companies and to ensure the continuity and replacement of appointments and the power to terminate (or to consent or give a general authorisation for the DGWS to terminate) an appointment in order to replace it;
- the power to impose conditions on the appointment and to veto modifications proposed by the DGWS in certain specified circumstances;
- the duty to make enforcement orders (and the exceptions to that duty), the procedure for enforcement orders and their validity and effect (certain functions relating to enforcement orders are exercisable concurrently with the Secretary of State as they relate to national security);

- the right to petition for special administration orders;
- enforcement of the general duties of the water undertakers (or consenting to or giving a general authorisation for the DGWS to enforce such duties) and the making of regulations on standards of performance;
- the power to institute proceedings for the offence of supplying water unfit for human consumption, to make regulations to prevent contamination and maintain quality and to appoint a technical assessor to evaluate supplies;
- the enforcement of the general duty to provide a sewerage system (or consenting or giving a general authorisation for the DGWS to enforce such duty), the making of regulations prescribing standards for sewerage services and the procedure for such regulations;
- the power to make regulations relating to charging by volume and to make provisions for billing disputes to be referred to the DGWS;
- authorising the giving of financial assistance to, or guaranteeing the financial obligations of (in each case with the consent of the Treasury), a company where a special administration order is in force; and
- authorising the compulsory purchase of land (in some circumstances this function is transferred exclusively to the Assembly, in others it is carried out concurrently with the Secretary of State) and the creation of rights and interests over land and consenting to, or giving a general authorisation for, the disposal of any protected land.

Those functions, powers and duties which remain with the Secretary of State under the WIA include the appointment of the DGWS and the duty to make merger references to the Competition Commission (''**CC**'') in certain specified circumstances. Nothing in the provisions for transferring functions to the Assembly affects the role of Ofwat, which retains the same regulatory functions and powers in respect of DCC as it possesses in respect of Regulated Companies in England.

Licences

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 which relate to limits on charges, information reporting requirements, various codes of practice, and other matters. The main provisions of DCC's licence, as set out in Chapter 9, are typical of those of all licences. The DGWS is responsible for monitoring compliance with the conditions of the licence and, where necessary, enforcing compliance through procedures laid down in the WIA (see ''*Enforcement Orders*'' below).

Termination of a licence

There are certain circumstances provided for in the WIA where a Regulated Company could cease to hold a licence for all or part of its area:

- a Regulated Company could consent to the making of a replacement appointment or variation, which changes its appointed area, and the DGWS has the authority to appoint a new licence holder;
- under condition O of the licence, where the first date at which the Secretary of State may terminate a licence is 2014 (provided at least 10 years' notice has been given);
- under the provisions of the Special Administration regime (the licence may be terminated and the Special Administrator transfer the business to a successor (see ''*Enforcement Orders*'' below)); or
- 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 the Secretary of State or DGWS is to determine what provision should be made for fixing 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 regards 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. Recently the threshold for large user insets has been reduced (in England but not yet in Wales) which will increase the number of large users that are able to qualify for inset appointments.

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 of certain proposed modifications by the Secretary of State, 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 CC. 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 CC.

A modification reference requires the CC 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 CC 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 CC's report will state whether any adverse effects on the public interest could be remedied or prevented by modification of the licence. If the CC 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.

The Secretary of State would also have the power, among others, to modify the conditions of the licence after an investigation under the UK Fair Trading Act 1973 into a monopoly or merger situation, if the CC concludes that matters investigated by it in relation to water or sewerage services amount to the existence of a monopoly or merger situation and operate, or may be expected to operate, against the public interest.

Enforcement Orders

The general duties of Regulated Companies are enforceable by the Secretary of State or the DGWS or both, although, in the case of DCC, certain of the enforcement duties, in as far as they relate to Wales, have been transferred to the Assembly. 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 Secretary of State.

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 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 which 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.

Special Administration Orders

The WIA contains provisions enabling the Secretary of State and the DGWS to secure the general continuity of water supply and sewerage services. In certain specified circumstances, the High Court (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, where any action does require the Court's leave, the consent of the special administrator is acceptable in its place (see "*Restrictions on the enforcement of security*" below).

A special administrator has extensive powers under the WIA similar to those of an administrator under the Insolvency Act, but with certain important differences. A special administrator would 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: (a) transferring to one or more different Regulated 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 (b) 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 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 agrees 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 transfer is effected by a transfer scheme which the special administrator puts 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 the right to seek a review by the DGWS of the Regulated Company's charges pursuant to an Interim Determination or a shipwreck clause (as defined below). 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: (i) the power to make appropriate grants or loans to achieve the purposes of the special administration order or 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 or the discharge of any other financial obligations in connection with any borrowings of the Regulated Company subject to a special administration order.

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. So far as exercisable in relation to Wales, the functions of the Secretary of State under Section 156 of the WIA are transferred to the Assembly. 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 1989 Act) 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 ensures that, in disposing of protected land, the Regulated Company retains sufficient rights and assets to enable a special administrator to manage the business of the Regulated Company and 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 with customers and shareholders). To this end there are certain procedures for the disposal of protected land and special rules apply to disposals by auction or formal tender and to disposals to certain associated companies. The rules applying to disposals to associated companies are more restrictive than those applying to other disposals. 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.

Security

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 DCC's Licence) restrict a Regulated Company's ability to dispose of protected land (as explained in

"*Protected Land*" above). Accordingly, a licence restricts a Regulated Company's ability to create a charge or mortgage over protected land or assets required for the operation of its business as a Regulated Company. In the case of DCC, the Issuer estimates that the vast majority of DCC's assets by value is tangible property which is protected land and/or assets required in the operation of DCC's business as a Regulated Company and cannot therefore be effectively secured. This necessarily affects the ability of DCC 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 to block the appointment of a conventional Insolvency Act administrator.

In addition, provisions in a Regulated Company's licence require the Regulated Company at all times:

- 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 order could be achieved; and
- to act in the manner best calculated to ensure that it has adequate: (i) financial resources and facilities; and (ii) management resources, to enable it to carry out its regulated activities.

These provisions may further limit the ability of DCC to grant security over its assets and may limit in practice the ability to enforce such security.

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 is functions). These restrictions continue once a special administration order is in force with some modification (see "*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 alia*, 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); however, notwithstanding this, 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. 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.

Enforcement of Security over Shares in DCC

Under the WIA, the enforcement of security over, and the subsequent sale of, directly or indirectly, the shares in any group company, including the holding company of a Regulated Company such as DCC, would not be subject to the restrictions described above in relation to the security over DCC'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 Guarantor Security or the security over, and subsequently any planned disposal of, the shares in DCC to a third party purchaser, would require consultation with the DGWS. In addition, depending on the circumstances, the merger control provisions referred to in "*Competition in the Water Industry – Merger Regime*" below could apply in respect of any such disposal.

Economic Regulation

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 generally allows companies to retain for a period any savings attributable to efficiency, thus creating incentives to make such gains.

K price limitation formula

The main instrument of economic regulation are 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 retail price index ("**RPI**") plus an adjustment factor which may be positive, negative or zero ("**K**"). K is a number set 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.

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 infrastructure charges 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.

Periodic reviews of K

K must be reviewed every five years (the "**periodic review**"). Following the last periodic review, new price limits took effect from 1 April 2000 and are set for the five year period from 2000 to 2005. The DGWS will next reset price limits in 2004 and these will come 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 "*Ofwat Letter*" in Appendix B).

Interim Determinations of K

The conditions of the licences provide 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 DCC's Licence an application for an Interim Determination of K may be made in respect of a Notified Item (see below) or a Relevant Change of Circumstance (see below).

A "**Notified Item**" is 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. Notified Items put forward by the DGWS in the determination of price limits for the period 2000 to 2005 were: (a) the costs and revenues associated with any difference in the number of domestic customers who opt to switch to measured charges ("**meter optants**") from that assumed by

the DGWS; (b) any net increase in bad debt and debt collection costs arising from the loss of the power to disconnect residential customers for non-payment from 1 April 2000; and (c) any additional administrative costs arising out of statutory obligations to offer protection from high metered bills to vulnerable groups of customers (with respect to Wales, regulations regarding the protection of vulnerable groups have not yet been implemented).

"**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); (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; and (c) the amounts assumed in K for the necessary costs of securing or facilitating compliance with a legal requirement or achieving a service standard where the Regulated Company has failed to: (i) carry out the necessary works; (ii) spend the amount which it was assumed would be spent; and (iii) achieve the stated purpose.

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 base cash flows for each year included in the timing (the "**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 DCC) this materiality threshold is reached where the sum of the net present values of (a) Base Cash Flows consisting of operating expenditure and/or loss of revenue calculated over 15 years and (b) 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 Base Cash Flows. The change is then made for the remainder of the period up to the start of the first charging year of the next periodic review. Condition B of the Licence sets out in detail the step-by-step methodology which the DGWS is required to apply.

Substantial Adverse or Favourable Effects – Shipwreck Clause

In addition, a 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 (the "**shipwreck clause**"). Less than half of the Regulated Companies' licences (including DCC's) currently contain such a provision, but on 31 January 2001 the DGWS published an open letter to the Managing Directors of Regulated Companies offering to reinsert the clause in their licences and on 11 April 2001, following this consultation, he published another such letter confirming that he intends to reinsert the clause into the licences of those Regulated Companies (including DCC) which accepted the offer (subject to the 28 day consultation period for all licence modifications).

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 CC. The CC 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 CC are binding on the DGWS.

Drinking Water and Environmental Regulation

The water industry is subject to numerous regulatory requirements concerning the protection of the environment and human health and safety. Responsibility for regulation of drinking water quality and environmental standards lies with the DWI and the EA respectively.

The DWI is part of the DETR and acts as a technical assessor on behalf of the Secretary of State in respect of the quality of drinking water supplies. It can 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 Secretary of State or the Director of Public Prosecutions for the offence of supplying water ''unfit for human consumption'', for example if discoloured or foul tasting water is supplied to customers.

The EA is responsible in England and Wales for the control of water pollution and the maintenance and improvement of the quality of controlled waters, including the regulation of discharges to those waters. The principal UK environmental legislation relevant to Regulated Companies includes the Water Resources Act 1991 (the ''**WRA**''), the Environmental Protection Act 1990 (the ''**EPA**'') and the WIA. The draft Water Bill proposes amendments to both the WRA and the WIA (see ''*The Draft Water Bill*'' below).

Under the WRA any discharge of trade or sewage effluent into controlled waters can only be carried out with a discharge consent from the EA or with some other lawful authority. The discharge consent system under the WRA is backed up by various criminal offences. It is a criminal offence to cause or knowingly permit polluting matter to enter controlled waters. 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 such works from the person who caused or knowingly permitted the pollution (and can also require that person to take the remedial action itself).

Sewerage undertakers are responsible under the WIA for regulating discharges of industrial effluent into sewers. In addition, discharges from sewage treatment works must be licensed by the EA. Contamination of controlled waters by discharge of non-compliant effluent from a treatment works may subject the sewerage undertaker to liability, including fines and clean-up costs. The EA publicises breaches by Regulated Companies of their discharge consents and brings prosecutions where necessary. Depending on developments in case law, sewerage undertakers may in future have to negotiate contracts with the owners of water courses in order to be able to discharge water into such water courses. The additional costs involved may be significant.

Liability may also arise in the future under Part IIA of the EPA which came into effect in England in April 2000 and is expected to be implemented in Wales later in 2001. The EPA (supported by statutory guidance), will introduce a regime to deal with the remediation of contaminated land. Under the regime, the causer or knowing permitter of the pollution (or, if that person cannot be found, the owner or occupier of the land) can be required to clean up contamination if it is causing, or there is a significant possibility of it causing, significant harm to the environment or human health or if pollution of controlled waters is being caused. Civil liability may also arise (under such heads of claim as nuisance and negligence) where contamination migrates into the environment at third party land and/or impacts upon human health, flora and fauna.

Depending on the type and volume of waste processed, certain sewage treatment works which employ biological treatment processes or deal with non-domestic hazardous wastes of over 10 tonnes per day will be subject to the new integrated pollution prevention and control regime (''**IPPC**'') which was introduced by the UK Pollution Prevention and Control Act 1999 and is being phased in across UK industry in the period to 2007. 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. This may give rise to increased expenditure.

The activities of the Regulated Companies are also affected by the requirements of EU Directives. The principal EU Directives currently in force relating to water and which have been given effect in UK law are the Urban Waste Water Treatment Directive (the ''**UWWTD**''), the Drinking Water Directive and the Bathing Water Directive. The purpose of the UWWTD is the reduction of pollution caused by urban sewage. The Drinking Water Directive seeks to protect human health from contaminated water, whilst the aim of the Bathing Water Directive is to ensure the quality of bathing water in order to protect public health and the environment. The Water Framework Directive which was agreed in October 2000 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. This Directive must be transposed into UK law by 2003 and is expected to have a significant impact on Regulated Companies in the longer term as Member States must aim to achieve ''good'' status for surface waters and ground water within the next fifteen years.

Any expenditure incurred by a Regulated Company necessitated by new legislation applying to it in its capacity as a water or sewerage operator, or by any change in consents as a result of any changes to existing EU directives, or adoption of future EU directives, would be eligible for consideration for an Interim Determination of K, or to be taken into account at a periodic review.

Competition in the Water Industry

Each Regulated Company effectively holds a geographic monopoly within its appointed area for the provision of public mains and water and sewerage services. There is certain limited competition, however, for the provision of water and sewerage services and the UK Government has indicated that it hopes 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 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 a specified geographical area within the other Regulated Company's appointed territory;
- common carriage – when a company supplies water or sewerage services to its customers using a Regulated Company's network. All Regulated Companies prepared draft network access codes during the course of 2000, however, no agreements for the provision of third party access have been announced as yet, either by existing Regulated Companies or new entrants; and
- 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.

In April 2000, the DETR published a consultation paper ''Competition in the Water Industry in England and Wales'' (the ''**Competition Consultation Paper**'') on ways to extend the scope for competition both through the methods set out above and by introducing further mechanisms as set out below:

- further lowering the threshold for inset appointments, time limiting inset appointments and allowing premises to be combined to meet the consumption limit for a large user inset;
- extending the obligation on Regulated Companies to allow connections to their water mains from outside their areas in response to requests by non-domestic customers as well as domestic customers (currently, Regulated Companies are only obliged to make such supplies outside their areas when requested by domestic customers);
- time limiting abstraction licences and liberalising trade in abstraction licences so that new entrants can enter the market for the provision of water (the provisions for which are contained in the draft Water Bill); and
- removing water companies' monopolies in making connections to water mains.

In addition, the Competition Consultation Paper put forward three more radical amendments to the existing regulatory regime:

- licensing – whereby potential new entrants could be licensed to supply water or sewerage services to any customer over a given size, rather than being restricted by the existing limitation of inset appointments;
- restructuring – where the key monopoly elements of the industry are separated out and competition is promoted at each level; and
- franchising – where statutory undertakers are required to seek bids for a franchise to operate the whole of their main operational functions.

On 17 April 2001 the DETR announced that it plans to issue a further consultation paper in the summer of 2001, inviting views on more detailed proposals for increased competition in the industry. Requisite legal provisions for these proposals will be incorporated in the draft Water Bill before it is introduced to Parliament.

The aim of the proposals is to provide a framework for competitors to enter the market in production (water abstraction and treatment) and retail activities (billing and customer services). New entrants to the market would apply to the DGWS for licences for production and/or retail activities and only licencees would be able to make common carriage arrangements with incumbent network operators.

Regulated Companies would remain monopoly network operators with responsibility for resource planning and as ''suppliers of last resort'' (a duty to supply water for domestic purposes to any customer and to provide alternative sources of supply when mains supplies fail). The cost to Regulated Companies of undertaking these activities would be taken into account in the charges they set new entrants for using their pipes and facilities.

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 between undertakings which may affect trade within the United Kingdom and which have as their object or effect the prevention, restriction or distortion of competition within the United Kingdom. The Chapter II Prohibition prohibits the abuse of a dominant position which may affect trade within the United Kingdom.

The DGWS has concurrent powers with the Director General of the Office of Fair Trading to apply and enforce the Competition Act 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 turnover of the Regulated Company involved for up to three years for infringing the Competition Act. Also any arrangement which infringes the Competition Act may be void and unenforceable and may give rise to claims for damages from third parties.

Merger Regime

The Secretary of State has a duty to refer to the CC mergers or proposed mergers between two or more Regulated Companies where the value of the gross assets of each of the Regulated Companies to be merged exceeds £30 million. In determining whether such a matter operates or may be expected to operate against the public interest, the CC must have regard to the desirability of giving effect to the principle that the DGWS's ability to make comparisons between different water companies should not be prejudiced.

In cases of an acquisition of a Regulated Company by a company which is not already a Regulated Company, general merger control rules apply. These may call for discussion with the Office of Fair Trading (''**OFT**'') as well as Ofwat. The Director General of Fair Trading has the power to investigate any merger within the jurisdiction of the UK merger regime. He advises the Secretary of State on whether the transaction should be referred to the CC for further investigation to determine if the arrangement will or may be expected to operate against the public interest. In giving his advice to the Secretary of State he will consult with Ofwat. Depending on the size of the parties involved, such mergers may require notification to the European Commission under the European Union's merger regime.

Monopoly Regime

Where it appears to the DGWS or the Director General of Fair Trading, the Secretary of State alone or together with another Minister, that a monopoly situation exists or may exist in relation to commercial activities connected with the supply of water or the provision of sewerage services he may refer the matter to the CC. These powers relate to both scale, or structural, monopolies as well as complex, or behavioural, monopolies. The CC will investigate the matter and, if a monopoly situation exists and there are effects adverse to the public interest the CC must consider what, if any, action should be taken to remedy or prevent them and may, if it thinks fit, recommend remedial action. The remedy may be implemented either by virtue of the monopolist giving appropriate undertakings or by an order from the Secretary of State.

The Draft Water Bill

On 6 November 2000 the UK Government published the consultation document "Water Bill – Consultation on draft legislation" (the "**Water Bill Consultation Paper**"). The consultation ran until 31 January 2000. This document and the draft Water Bill draw together the results of a number of previous consultation exercises including the DTI July 1998 white paper, "A Fair Deal for Customers – Modernising the Framework for Utility Regulation" (the "**White Paper**") and the Competition Consultation Paper. The White Paper set out proposals relating to the water sector which were originally reflected in the Utilities Bill but which were withdrawn and are now reflected in the draft Water Bill. The draft Water Bill has three main elements:

- reform of abstraction licensing and promotion of greater water conservation by water companies;
- the re-introduction of the provisions of new regulatory arrangements for water aiming to put the consumer at the heart of the regulatory process and to make regulation more open and accountable which were removed from the Utilities Bill; and
- other changes to the regulatory system for water.

The Water Bill Consultation Paper contains both firm proposals, which are provided for in the draft Water Bill, and a discussion of "work in progress" which may be included in the future draft legislation when the bill is introduced.

Firm proposals made in the Bill include:

- Financial Penalties for Breaches of Statutory Requirements

  A power for the DGWS, the Secretary of State and the Assembly to impose financial penalties on a Regulated Company for contraventions of its licence, statutory or other requirements including performance standards. The penalty must be reasonable in all the circumstances and be not more than 10 per cent. of a Regulated Company's turnover. A financial penalty may not be imposed under this provision for an infringement if it is more appropriate to proceed under the Competition Act.

- Consumer Objective

  An amendment to the primary duties of the Secretary of State, the Assembly and the DGWS to introduce a new consumer objective to protect the interests of consumers of regulated water and sewerage services, wherever appropriate, by promoting effective competition. In addition a modification to the regulators' duty to secure that Regulated Companies are able to finance the proper carrying out of their functions by removing the words "in particular by securing reasonable returns on their capital".

It was intended that the results of the Competition Consultation Paper be included in the draft Water Bill. However, in the light of responses to it and to industry developments, the UK Government concluded that further work on options for extending competition in the water industry needed to be undertaken. In its statement of 17 April 2001, the UK Government announced that a further consultation paper, setting out detailed proposals for increased competition in the industry, will be issued in the summer of 2001 (as further described above). It is proposed that the legal provisions underpinning such proposals will be included in the draft Water Bill.

On 31 January 2001, Ofwat published its response to the Consultation Paper. In its response, Ofwat welcomed the proposals in the draft Water Bill and stated that in particular it shared the objective of placing customers at the heart of regulation. However, Ofwat stated competition also has potential benefits for consumers and that the proposals in the consultation paper are incomplete without the UK Government's proposals to promote further competition. More recently, the DGWS, in a speech in March 2001, suggested that progress could be made in introducing competition in the industry by introducing a licence recognising the different roles within the public water supply system: supply, distribution and retail.

Other subjects which are currently being considered, and which could lead to legislative provisions relevant to Regulated Companies, include:

- measures to improve the availability to customers of information on company performance; and

- the application of “economic instruments” to water abstraction (e.g. “incentive” pricing, tradable water rights).

No mention of the Bill was made in the Queen’s speech in December 2000 and there is no proposed timetable for the Bill to pass through Parliament.

Customer Interests

The DGWS is responsible for protecting the interests of customers. It monitors the performance and level of service of Regulated Companies and the implementation of a “guaranteed standards” scheme in respect of customer care.

Customer Service Committees

Under the WIA, the DGWS is required to establish regional Customer Service Committees (the “**CSCs**”). Each of the ten CSCs has a Chairman and between ten and twenty 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 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 ten 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.

Guaranteed Standards

If a Regulated Company does not meet any of its legally guaranteed standards under Ofwat’s guaranteed standards scheme, the customer is entitled to compensation, normally in the region of £20 for domestic customers and £50 for business customers within 10 working days of the incident. This scheme has not yet been formally implemented in Wales, however DCC does operate a substantially similar scheme which provides compensation, again normally in the region of £20 for domestic customers and £50 for business customers, where breach of guaranteed standards has occurred.

CHAPTER 9

THE FINANCING GROUP

THE FINANCING GROUP

The sole purpose for the creation of the Financing Group is to facilitate the refinancing and future financing of the operating and capital requirements of DCC through, *inter alia*, the issuance of Bonds and other financial indebtedness, from time to time by the Issuer. DCC will be funded through loans made by the Issuer pursuant to Intercompany Loan Agreements and through certain other available resources (see Chapter 4 under "*Intercompany Loan Agreements*" and "*Additional Resources Available*").

THE ISSUER

Introduction

Dwr Cymru (Financing) Limited was incorporated in the Cayman Islands on 15 February 2001 as an exempted company with limited liability, with registered number 108127. The Issuer is a subsidiary of Holdings. The Issuer has no subsidiaries.

The Issuer's authorised share capital is £50,000 divided into 50,000 ordinary shares of £1 each, 30,000 of which have been issued and are fully paid-up. The remaining 20,000 ordinary shares have been authorised but are not yet in issue. As at the date of this Information Memorandum, the Issuer has no other equity or debt capital.

The Issuer's registered office is at P.O. Box 309, Ugland House, South Church Street, George Town, Grand Cayman, Cayman Islands, and its secretary is Mrs. Sally Jones. The Issuer's directors are Mr. John Michael Barham and Mr. Daniel Charl Stephanus Oosthuizen (see "*DCC Directors and Secretary*" below for further details) and the Issuer's registered business address is PO Box 295, Alexandra Gate, Rover Way, Cardiff CF24 5UE.

The Issuer will be managed in such a way as to ensure that it is resident for tax purposes in the United Kingdom.

The Issuer has no employees nor does it own any tangible or physical assets (including, in particular, any real property). Administration and treasury operations are conducted on its behalf by DCC and certain third parties including Maples and Calder.

The Issuer, 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 Issuer's auditors will be PricewaterhouseCoopers, chartered accountants. Its first audited accounts will be drawn at and to 31 March 2002. The text of the auditor's report dated 4 May 2001 prepared by the Issuer's auditors is contained in Appendix G.

Capitalisation and Indebtedness Statement of the Issuer

The capitalisation of the Issuer as at the date of this Information Memorandum is as follows:

Share Capital	**£**
Authorised:	
50,000 ordinary shares of £1 each	50,000
Issued:	
30,000 ordinary shares of £1 each	30,000
Total capitalisation and indebtedness	30,000

In addition to the Bonds issued on the Initial Issue Date, on or before the Initial Issue Date, the Issuer will enter into (a) the Initial Liquidity Facility Agreement to enable it to borrow moneys in order to fund Liquidity Shortfalls in respect of the first Series of Bonds issued on such date; (b) the Initial Hedging Agreements in accordance with the Hedging Strategy; and (c) an Authorised Loan Facility (see Chapter 4 under "*Summary of the Finance Documents*").

Save for the foregoing, at the date of this Information Memorandum, the Issuer has no borrowings or indebtedness in the nature of borrowings (including loan capital issued or created but unissued), term loans, liabilities under acceptances or acceptance credits, mortgages, charges or guarantees or other contingent liabilities.

HOLDINGS

Dŵr Cymru (Holdings) Limited was incorporated in England and Wales on 23 March 2000 as a limited liability company under the Companies Act, with registered number 3954867 under the name of WW29 Limited. WW29 Limited passed a special resolution to change its name on 9 January 2001 and its new name Dŵr Cymru (Holdings) Limited was registered at Companies House on 10 January 2001.

Holdings is a wholly owned subsidiary of HUH. Holdings owns all of the 200 million 7 per cent. preference shares of £1 each in DCC and all of the 109,876,374 ordinary shares of £1 each in DCC. Holdings also owns all of the 30,000 ordinary shares of £1 each in the Issuer. Apart from DCC and the Issuer, Holdings has no other subsidiaries.

Holdings' authorised capital is £1,000 divided into 1,000 ordinary shares of £1 each and 30,000 redeemable preferred ordinary shares of £1 each. Holdings has the power under its Memorandum of Association to divide this capital into several classes, and to attach thereto any preferential, deferred, qualified or other special rights, privileges, restrictions or conditions. One ordinary share of £1 has been issued and is fully paid-up and is held by HUH; 30,000 redeemable preferred ordinary shares of £1 each have been issued and fully paid-up and are held by Glas Securities.

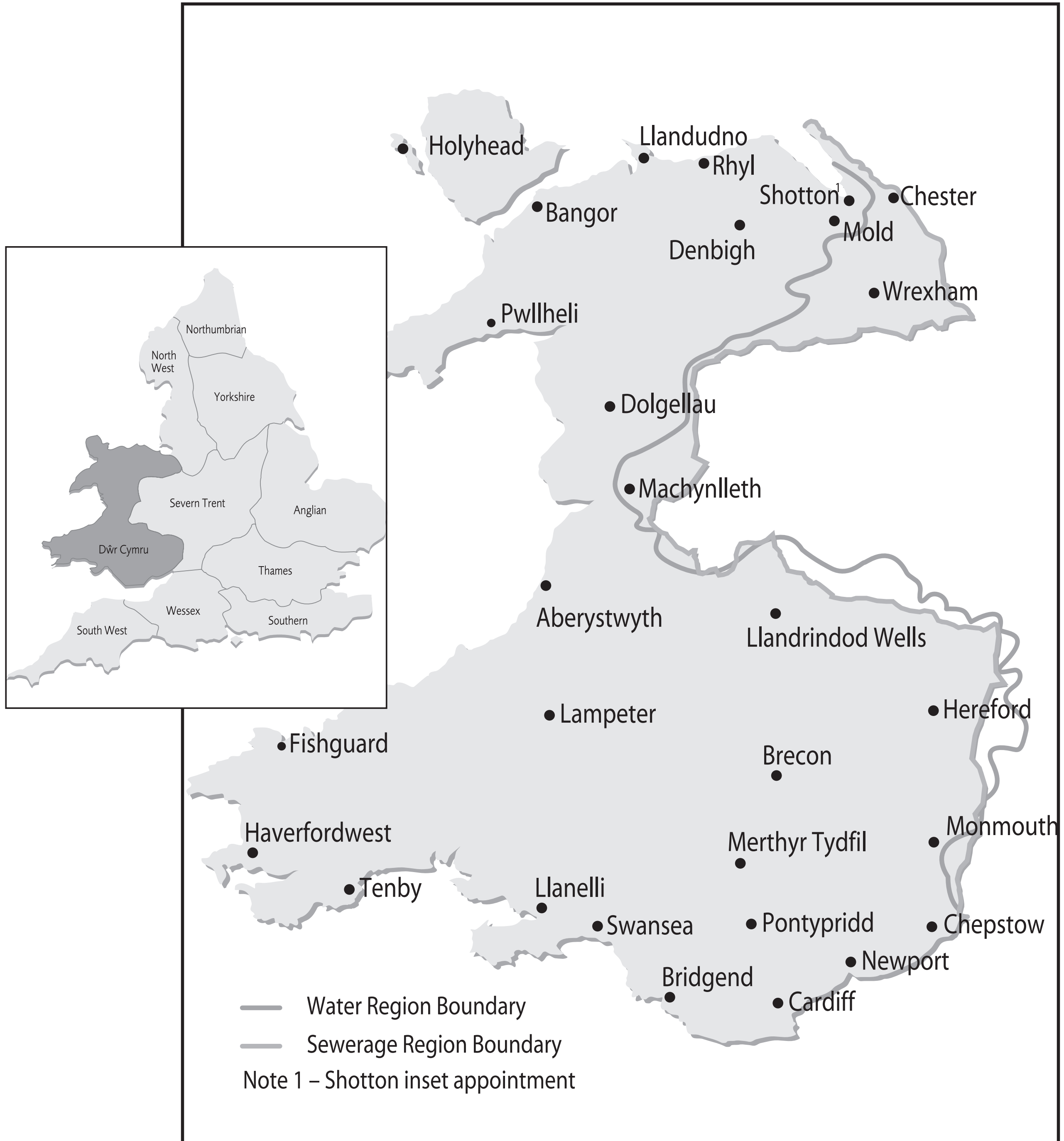
Holdings' registered office is at PO Box 295, Alexandra Gate, Rover Way, Cardiff, CF24 5UE and its secretary is Mrs. Sally Jones. Holdings' directors are Dr. Michael Peter Brooker, Mr. Daniel Charl Stephanus Oosthuizen and Mr. Robert Arthur Symons (see "*DCC Directors and Secretary*" below for further details), and their business address is PO Box 295, Alexander Gate, Rover Way, Cardiff CF24 5UE.

Holdings has no employees nor does it own any tangible or physical assets (including, in particular, any real property) other than its shares in DCC and the Issuer. Administration and treasury operations are conducted on its behalf by DCC and certain third parties.

The principal activity of Holdings is to hold the shares of DCC and the Issuer, and to enter into all documents incidental to the Programme. Holdings has the power under its memorandum and articles of association to enter into the proposed transaction documents to which it is a party and the directors have authority under the company's articles of association to exercise that power on its behalf.

Holdings' auditors are PricewaterhouseCoopers, chartered accountants. No statutory accounts have been prepared or delivered to the Registrar of Companies in England and Wales since Holdings' incorporation. Its first statutory accounts will be drawn at and to 31 March 2001, and its accounting reference date will be 31 March of each year.

DCC
Map of Licence Area



Introduction

Dŵr Cymru Cyfyngedig was incorporated on 1 April 1989 and is a wholly-owned subsidiary of Holdings, which in turn is owned by HUH.

The principal activity of DCC is the supply of water and the treatment and disposal of sewage. The area served is shown in the map above and is described below.

As a Regulated Company under the WIA, DCC is restricted from disposing or otherwise encumbering its ''protected land'' and is subject to a special insolvency regime as set out in the WIA (see Chapter 8 under ''*Protected Land*'' and ''*Special Administration Orders*'').

For the year ended 31 March 2000, total water and sewerage turnover (including intra- and inter-segment turnover) was £476.9 million, yielding gross profits before interest and exceptional items of £186.1 million.

The Area Served

DCC's water supply area covers most of Wales as well as parts of Herefordshire and Gloucestershire in England. DCC's sewerage area covers most of Wales and parts of Herefordshire, Gloucestershire, Cheshire, Shropshire and the Wirral. The sewerage boundary includes the Dee and Wye catchments in England but excludes the catchment of the River Severn in Mid Wales.

There is an inset appointment to cover the supply of water to Shotten Paper.

Economic, Social and Demographic Factors

DCC is the sixth largest water service and sewerage company in England and Wales (based on turnover), serving some 1.2 million domestic residences and 111,000 business premises in Wales and parts of England. DCC's service area has a resident population of approximately 3 million people, two thirds of which live in the relatively more industrial southern and northeastern parts of the region. The largest centres of population include Cardiff, Swansea and Newport in the south and Chester and Wrexham in the northeast. DCC provides services not only to these centres but also to the sparsely populated parts of the region.

DCC supplies water in a region of some 20,400 square kilometres with an estimated connected population of some 2.9 million, and provides sewerage services in a region of some 21,300 square kilometres with an estimated connected population of some 3.0 million. In addition, it has the infrastructure in place to provide services to the region's many visitors. Most of the premises served by DCC's sewerage services also receive water supplies from DCC. The balance receive water supplies mainly from Dee Valley Water plc.

Metered water supplies and measured discharges for sewage and trade effluent are influenced by the economic climate. Metered turnover in the year ended 31 March 2000 year was divided equally between the first and second half years.

Water

In the year ended 31 March 2000, DCC put into supply on average 1,050 megalitres (''**Ml**'') of water per day. During the same year, DCC also supplied approximately 350 Ml/day of untreated water from the Elan Valley reservoirs to Severn Trent Water Limited under a bulk supply agreement.

Of the water abstracted by DCC for public supply, 42 per cent. is abstracted directly from supply reservoirs and 55 per cent. is abstracted from rivers, streams and springs. Because of the geological characteristics of the region covered by its Licence, DCC takes only 3 per cent. of its abstraction from underground sources.

Much of the region covered by the Licence is sparsely populated which creates particular difficulties for water supply. Whilst there is generally no significant seasonal fluctuation in the total water put into supply, the quantity of treated water supplied does vary during the year and this can be due to a number of factors such as dry weather, the influx of summer visitors and burst pipes due to freeze/thaw cycles during winter months.

Abstracted water is treated at water treatment works prior to being distributed through water mains and service pipes to the public. All of the water produced for domestic use is treated. However, DCC has a number of special bulk supply arrangements to supply untreated or partially treated water to customers in the steel, oil, electricity, brewing and paper industries. These arrangements account for approximately 11 per cent. of the water supplied to DCC's customers.

Water is treated at 113 water treatment works and is distributed to more than 1.3 million premises through a network of approximately 26,800 kilometres of mains, more than 620 water pumping stations and more than 740 service reservoirs. The length of the mains operated by DCC is high in relation to the number of premises served compared to other water companies, reflecting the widely spread population.

In the year ended 31 March 2000, on average 1050 Ml/day of water (including the water put into supply pursuant to bulk supply arrangements) was put into distribution and 288 Ml/day was estimated as lost through leakage. About three quarters of this leakage is estimated to be from DCC's pipes and one quarter from pipes owned by households and businesses. DCC has set a target to reduce leakage to 242 Ml/day by the end of the year ending 31 March 2002. This equates to reducing the estimated rate of leakage from 10.8m^3/km/day in the year ended 31 March 2000 to 8.8m^3/km/day by 31 March 2002. In the year ended 31 March 2000 the average estimated rate of leakage for the water industry in England and Wales was 10.1m^3/km/day.

Most of DCC's mains are constructed of iron, asbestos/cement and plastics, with iron being the most common material. The average age of the mains is approximately 55 years. The replacement and repair programme, which is reflected in Ofwat's 1999 determination, provides for the replacement of approximately 500 km of pipeline per annum.

To assess compliance, water quality is monitored by DCC through a programme of regular sampling and analysis. Sampling of water supplies is carried out in accordance with the Water Supply (Water Quality) Regulations 2000 which sets out the number of samples to be taken depending on the volume of water produced or the population served. In addition all service reservoirs (tanks) have to be sampled weekly. Analysis at water treatment works and service reservoirs concentrates on bacteriological sampling, to ensure that the water has been adequately disinfected and is safe to drink.

A more sophisticated analysis is made at the point of consumption (i.e. the customer's tap). This analysis includes all chemical and bacteriological parameters as prescribed by the Water Supply (Water Quality) Regulations and the frequency that samples are taken and the analysis made depends on the population size. Results of analysis falling outside the prescribed parameters are investigated and reported on a monthly basis to the DWI which has the regulatory powers to enforce improvements unless remedial action has already been taken.

DCC operates a quality assurance system approved to BSi standard ISO 9002. DCC has approved procedures for the total process from source to point of consumption; these are used to monitor the daily activities which control water quality. These procedures are audited by BSi on a six monthly basis.

Sewerage

DCC receives an estimated flow of 560 Ml/day of returned sewage into its sewerage network. This includes an average volume of 74 Ml/day of trade effluent from 780 industrial customers, including those in the metals, food and drink and livestock businesses, who have permission to discharge trade effluent. These figures exclude storm flows and any infiltration. A number of factors, including rainfall, may cause flows within DCC's sewerage network to vary from time to time. In particular, in certain areas of the sewerage region, notably on the coast, an influx of visitors during the summer holiday period contributes to an increase in the sewage flow.

DCC is responsible for the operation and maintenance of 850 sewage treatment works, 50 coastal outfalls and approximately 17,500 kilometres of sewers receiving foul and surface water through a mixture of combined, separate and partially separate drainage systems. These systems serve in some cases only a few remote houses and in others whole towns and major conurbations. There are approximately 1,645 sewage pumping stations within the sewerage region which form an integral part of the sewerage system.

Approximately three quarters of the sewage collected in DCC's systems is treated at its sewage treatment works. The remainder is sent to coastal or estuarial outfalls where at present DCC has limited or no treatment facilities.

Over the five-year period from 31 March 1995 to 31 March 2000, DCC completed the construction of 22 new sewage treatment works together with 73 extension or improvement schemes at sewage treatment works. The total cost of the work was approximately £650m of the £1.25 billion capital expenditure of DCC for the period. As a result of this investment, by 31 March 2000, DCC was providing full biological treatment to approximately 70 per cent. of the sewage it collected compared

with 55 per cent. as at 31 March 1995. The current investment programme which addresses quality improvements at approximately 200 sewage treatment works aims to ensure that, by 31 March 2005, DCC will provide full biological treatment to over 98 per cent. of the sewage it collects.

Annually, DCC disposes of sewage sludge containing an estimated 42,000 tonnes of dry solids. This figure is set to rise to over 70,000 tonnes when all the new works have been completed. The largest is at Cardiff which will contribute 16,000 tonnes p.a. Approximately 88 per cent. of this is disposed of on agricultural land. The majority of the sludge that is unsuitable for disposal on agricultural land is disposed of in landfill sites.

The disposal of sludge produced by wastewater treatment works is strictly controlled. Disposal to landfill sites is becoming restricted due to the lack of available local sites. 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 an EU directive, compliance with which is monitored by the EA.

Regulation

DCC is principally regulated under the provisions of the WIA. The Assembly, the Secretary of State for the Environment, Transport and the Regions, and the DGWS are the principal regulators of DCC. (See Chapter 8: ''*Water Regulation*'' for full details on the regulation of Regulated Companies, including DCC.)

The main provisions of DCC's Licence are as follows:

- the restriction of the annual increase in a basket of standard charges to the price cap formula, RPI+K;
- periodic reviews of K every five years by a determination made by the DGWS;
- Interim Determinations of K by the DGWS between periodic reviews. At present, the specified circumstances which may trigger an Interim Determination for DCC include a new or changed legal requirement, variations in values received or expected to be received from disposals of land, a net increase in bad debts due to the loss of power to disconnect, and a higher rate of domestic optional metering than that anticipated by the DGWS in his recent periodic review determination;
- provisions which enable DCC to require the DGWS to refer a periodic review determination or an Interim Determination to the CC for re-determination;
- requirements relating to the ''financial ring-fencing'' of the regulated business and transactions with associated companies, including the payment of dividends, and a requirement that DCC has at its disposal sufficient financial and managerial resources to carry out its regulated activities (including any investment programme necessary to fulfil licence obligations) and the ''ring-fencing'' of land and other assets;
- a requirement that DCC obtain a legally enforceable undertaking from its parent company stipulating that it refrain from any action which would prejudice the ability of DCC to comply with its obligations under the Licence and the WIA;
- a provision that the Secretary of State may only terminate the Licence after 25 years have elapsed since the day on which the functions of the Welsh Water Authority were transferred to DCC in 1989, and by the giving of at least 10 years notice to that effect;
- a requirement to prepare and publish separate accounts, including on a current cost accounting basis showing separately its appointed business from all other businesses and activities; and
- a further requirement that the regulated business neither gives to, nor receives from, any other business or activity of DCC or any other company within the Group, any cross-subsidy, whether those businesses are regulated by the Licence or not and that any transaction with any other company within the Group be on arm's length terms.

Other conditions of the Licence cover obligations relating to the calculation and application of ''infrastructure charges'', the preparation of charges schemes, the duty not to show undue preference or discrimination in the setting of charges, the provision of information to the DGWS, the preparation of Codes of Practice for general customer matters, disconnection and leakage, service standards and targets, the preparation of Underground Asset Management Plans, the payment of fees to Ofwat and compensation for customers in the event of interruptions to supply during a drought.

A number of modifications to DCC's Licence have been proposed by Ofwat (see Chapter 11 under "*Glas and the Regulator*").

Water Resources

DCC benefits from a combination of high annual rainfall and topographical and geological conditions which favour the catchment and storage of water. In north and mid Wales, which have significant upland areas, peat covered upper slopes combined with impervious rock facilitate the collection and storage of water. In northeast Wales and parts of South Wales sandstone and limestone form aquifers capable of providing local supplies of water.

Pollution Control

Regulatory control of discharges to the environment is undertaken by the EA which regularly samples discharges from treatment works. The aquatic environment in Wales is of high quality, with 92 per cent. of rivers of the very highest quality and 53 bathing beaches and marinas attracting the European Blue Flag or Green Coast awards (controlled by the Keep Wales Tidy Group). As part of improvements in efficiency and effectiveness most of the primary assets are remotely monitored to ensure that quality standards are met.

Insurance

DCC maintains insurance cover consistent with the generally accepted practices of prudent water and sewerage undertakers. This includes all risks property damage and third party liability insurance.

All insurance is arranged in the name of DCC and its subsidiary undertakings. There is also provision for 'joint names' cover for third parties where appropriate.

The All Risks Property Damage Policy provides cover for all risks of loss or damage, including fire and theft. The policy provides cover for consequential losses arising from damage to or loss of assets including loss of revenue and additional costs reasonably incurred. The policy covers property of every description belonging to DCC or for which DCC is responsible. The assets are covered up to their full replacement value of £11.8 billion. Business interruption is covered up to £50 million. There is a separate policy in force for mechanical and electrical engineering breakdown up to a limit of £30 million. Property damage caused by fire or explosion arising from an act of terrorism is also covered under a separate policy.

Comprehensive combined third party liability policies fully underwritten in the London Insurance Market are also maintained by DCC. These policies include public and products liability insurance. The insurance is placed under two arrangements: (a) a Primary Combined Liability Policy with AXA Corporate Solution Risks with an indemnity limit of £5 million; and (b) separate Excess Layer Public and Products Liability Policies placed with various composite insurers with excess indemnity limits of up to £100m.

Rates and Billings

Water supply and sewerage services are charged separately and, therefore, charges are set so as to reflect the average costs of providing each service for each class of customers. The average household bill within the region supplied by DCC for the year to 31 March 2001 was £304, comprising £136 for water supply and £168 for sewerage services. Currently 89 per cent. of turnover in respect of water and sewerage customers relates to supplies to unmetered customers. Of the remainder, 7 per cent. of household customers pay a standing charge and 4 per cent. pay by meter.

Customers with unmetered supplies are billed primarily in advance on an annual basis with payment 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.

Most domestic customers are unmetered, and the bill is based on the rateable value of their home. Although the domestic rating system was discontinued in 1990 (under the provisions of the UK Local Government Finance Act 1988), water companies were originally allowed to continue to use rateable values for charging until 1 April 2000 under the WIA. More recently, following a review of water and sewerage charges in England and Wales, the UK Government has decided to allow companies to continue using the system after that date. At the same time it proposed changes designed to encourage the use of meters on domestic properties.

These changes have been implemented by the UK Water Industry Act 1999 which grants domestic customers the right:

- to resist water metering in their current homes where they are not using water for non-essential purposes;
- to have a free meter installed if they wish to have one, where this is practicable; and
- where they have taken up the right to have a free meter installed, to revert to an unmetered basis of charging within 12 months if they so choose.

In addition, new provisions of the WIA as amended by the UK Water Industry Act 1999 serve to:

- prevent disconnection of domestic customers and other protected premises for non-payment;
- empower the Secretary of State to make provisions which protect vulnerable customers with high essential water use, who live in homes with meters, from higher than average bills (these provisions have not yet been implemented in Wales but are expected to be implemented); and
- prevent charges schemes from taking effect until approved by the DGWS and give the DGWS a duty to take into account guidance from the Secretary of State.

Metered customers in DCC's licensed area receive water and/or sewerage bills which are based on the amount of water used. Approximately 15 per cent. of DCC's customers receive metered supply producing 28 per cent. of DCC's total turnover.

Metered domestic customers of DCC receive an allowance of 5 per cent. for water not discharged to the sewer and certain industrial/commercial metered customers receive a higher allowance dependent on water not discharged to the sewer. As from 1 April 2001 all industrial/commercial metered customers of DCC will receive a minimum allowance of 5 per cent.

Most industrial and other non-domestic supplies are charged on the basis of the metered supply of water to the premises together with a fixed or minimum charge, based on the size of the meter serving the premises. Where a customer receives a metered water supply, sewerage charges are based on volume of water supplied. Charges for connection are generally set on a standard tariff basis. Trade effluent is normally charged on a formula basis taking account of the volume of effluent, its strength and costs of removal and treatment. No direct charge is made for highway drainage, the cost of which is recovered through sewerage charges to customers as a whole.

Collections

DCC offers customers a variety of payment options for settling charges for water supply and sewerage services. Domestic customers are offered the widest range of options aimed at facilitating collection of debt in a manner appropriate to their circumstances. Options range from offering discounts for annual payments in advance, payment by direct debit or using booklets and payment cards, through to doorstep collections and recourse to court procedures in appropriate circumstances. Disconnection of domestic customers from the water supply network for failure to pay charges is prohibited following the introduction of the UK Water Industry Act 1999. Industrial and commercial customers are subject to a range of actions, ranging through to disconnection where persistent failure to settle charges occurs.

DCC's total bad debt charge for the year to 31 March 2000 amounted to £30.0 million, including an exceptional charge of £20.0 million arising following the UK Government's decision to ban disconnection of domestic water customers, and its ruling restricting the use of prepayment water meter devices. After excluding the exceptional charge, the underlying bad debt charge for the year was £10.0 million on turnover of £476.9 million.

Capital Investment Programme

DCC has just completed a five year £1.25 billion capital investment programme up to 31 March 2000. The capital programme was driven in part by the EU Bathing Water Directive and the UWWTD which accounted for some £650 million of the total investment.

In the current five year period from 1 April 2000 to 31 March 2005, DCC plans to invest a further £1.1 billion (at May 1999 price levels) in capital projects. The emphasis is again on environmental improvements accounting for just over £600 million. However, the balance of the programme is somewhat different with over half the environmental programme being focused on reducing the frequency of storm spills from the sewerage system into rivers and estuaries and along the coast.

The five year programme is intended to deliver quality improvements at approximately 200 sewerage treatment works. Compliance with the UWWTD required that all works over 15,000 population equivalent (''**pe**'') (a measure that expresses the load to be treated from industrial and imported effluents in terms of the equivalent number of population) were completed by 31 December 2000. Therefore the current programme concentrates on the smaller works between 2,000 and 15,000 pe that are required to be completed by 31 December 2005.

The water treatment quality improvement programme was virtually completed in the previous five year programme. The current five year programme comprises improvements at nine works. Improvements continue at an increased rate to the water distribution network with rehabilitation/ replacement of approximately 2,500km of water mains planned. In addition, the current capital programme includes projects to address:

- above and below ground asset maintenance;
- water resources and security of water supply;
- reduction in leakage and improved water pressure levels;
- reduction in flooding from sewers;
- provision of new water mains and sewers for new development; and
- installation of approximately 200,000 water meters mainly for domestic customers.

Weather/Force Majeure

Water resources are generally adequate to meet forecast demand. DCC has been able to maintain supplies with only limited restrictions (for example, hosepipe bans) even in exceptional drought conditions such as those which prevailed in 1984, 1989, 1990 and 1995. Approximately one-quarter of the total water abstracted by DCC is supplied untreated to Severn Trent Water Limited under a bulk supply agreement.

Employees

DCC currently employs approximately 130 employees. The employees of DCC do not include those employees who provide services to DCC under existing service contracts and other arrangements, who were previously employed by HSL (and upon formalisation of the novation of the ITAs to Logica will be employed by Logica) or members of the Hyder Group and number approximately 370.

When the OSA and the CSA were awarded to United Utilities Operational Services Limited and Thames Water Services Limited respectively (see Chapter 12: ''*Procurement and Outsourcing*''), approximately 1,230 employees were transferred across from DCC by operation of the Transfer of Undertakings (Protection of Employment) Regulations 1981 (''**TUPE**'') or otherwise. Approximately 175 employees also transferred from members of the Hyder Group under the OSA and CSA by operation of TUPE or otherwise.

Employees of DCC currently participate in a number of pension schemes namely, the Hyder Water Pension Scheme, the Mirror Image Pension Scheme, the South Wales Electricity Group section of the Electricity Supply Pension Scheme, the Acer Group Pension Scheme and the Infralec 1992 Pension Scheme.

Following the transfer of 1,230 employees to the successful tenderers under the OSA and the CSA and the sale of DCC, the 130 remaining employees of DCC together with those transferred under the OSA and the CSA will stay in their current scheme for a brief transitional period. Thereafter, it is likely that new schemes will be established by DCC and the successful tenderers offering the employees similar past and future benefits.

Alternatively, if Inland Revenue approval is obtained to continue the Hyder Water Pension Scheme as a centralised scheme for associated employers (on a permanent community of interest basis) and agreement is reached between Glas and WPDH, DCC may take over responsibility for the Hyder Water Pension Scheme and the Mirror Image Pension Scheme. The Hyder Water Pension Scheme will be open to employees of DCC and transferred water employees of the Operator and the Service Provider respectively under the OSA and the CSA, with DCC acting as principal employer under the scheme. DCC employees who are members of the Mirror Image Pension Scheme will remain members of this scheme while they are employed by DCC and until the scheme is wound up (wind up is expected 31 March 2002).

Over the past few years a number of voluntary severance proposals have been made by DCC. A substantial number of staff were made redundant during the course of 2000 and the first few months of 2001. Enhanced redundancy terms, including enhanced pension payments, were offered to employees who accepted the voluntary severance package. The pension costs involved in redundancies from November 2000 are being met by the Hyder Water Pension Scheme.

Due to administrative oversight, DCC was not named on the contracting-out certificates for the pension schemes in which it participates and has not executed deeds of adherence in respect of its participation in such schemes. These omissions are in the course of being rectified but will be subject to the approval of the Inland Revenue.

Directors and Secretary

The directors and the secretary of DCC are set out below:

Officer	Appointment Type	Appointed
Dr. Michael Peter Brooker	Managing Executive Director	31 August 1989
Mr. Richard James Illidge	Executive Director	1 January 1996
Mrs. Sally Jones	Company Secretary	30 March 2001
Mr. Mark Steven Lynch	Executive Director	18 September 2000
Mr. Gerwyn John Miles	Executive Director	12 March 1998
Mr. Patrick Brendan Moriarty	Non-Executive Director	1 October 1996
Mr. Daniel Charl Stephanus Oosthuizen	Executive Director	13 December 2000
Mr. Robert Arthur Symons	Executive Director	13 December 2000
Mr. David Hugh Thomas	Non-Executive Director	1 October 1996
Mr. Jeffrey David Williams	Executive Director	12 May 1999

The business address of each of the above is Plas y Ffynnon, Cambrian Way, Brecon, Powys LD3 7HP (the registered and head office of DCC). On the completion of the Share Purchase Agreement, it is anticipated that, other than Dr. Michael Brooker, each of the above directors and secretary will resign and that new directors will be appointed. The new directors will be the same as the directors of Glas. See Chapter 11 under "*Incorporation, Board of Directors and Management*" for their names and biographies.

Dr. Michael Peter Brooker

Dr. Brooker has been a director of DCC since privatisation in 1989 and became Managing Director in July 1996. Since joining DCC in 1980 he has held a number of senior positions in the company.

Subsidiaries

The only subsidiary of DCC is WWUF, which was incorporated in England and Wales on 8 November 1993 as a public limited company under the Companies Act under the name Takeadvance PLC and subsequently changed its name to Welsh Water Utilities Finance PLC. Its registered number is 2869784. It was incorporated with a primary purpose as an investment company providing long term funding for the activities of DCC. All of the WWUF Sterling Bonds issued by it have been repurchased. (See Chapter 3: "*History and Background*".) It is intended that no further activities will be undertaken by it and that it will become a dormant company within the meaning of Section 249AA of the Companies Act.

DCC FINANCIAL INFORMATION

Financial Statements

Attached as Appendix D to this Information Memorandum are the audited accounts of DCC as at 31 March 2000 and, as Appendix E, the unaudited accounts to 31 December 2000. In addition, attached as Appendix F is a pro forma unaudited balance sheet of DCC as at 31 December 2000.

Capitalisation and Indebtedness Statement of DCC

The following table sets out the unaudited consolidated capital and reserves and indebtedness of DCC as at 31 December 2000:

	Unaudited as at 31 December 2000
	£m
Capital and reserves	
Share Capital	
Authorised	
Ordinary shares of £1 each	301.1
Preference Shares of £1 each	200.0
Allotted, called up and full paid	
Ordinary shares of £1 each	276.1
Preference Shares of £1 each	200.0
Reserves	719.2
Equity shareholders' funds	995.3
Non-equity shareholders' funds	200.0
Total shareholders' funds[1]	1195.3
Indebtedness	
Unsecured:	
Amounts falling due within one year[2]	161.9
Amounts falling due after more than one year	507.4
Obligations under finance leases:	
Amounts falling due within one year	1.5
Amounts falling due after more than one year	263.9
Total Indebtedness[1]	934.7

Notes:

(1) **Material changes in shareholders' funds and indebtedness since 31 December 2000**

On 17 January 2001, DCC drew down £641 million under the Bridge Facility. This money was utilised as follows:

(i) the repayment of the intercompany balance with WWUF in respect of the £200 million WWUF Sterling Bonds and a £11.9 million penalty for early repayment; and

(ii) the repurchase from HUH of 166.2 million of its £1 ordinary shares for £428.7 million.

The repurchase of DCC's shares resulted in a reduction in reserves of £428.7 million, the cancellation of 166.2 million £1 ordinary shares and the creation of a capital redemption reserve of £166.2 million.

On 7 March 2001 DCC made a further £208 million draw down under the Bridge Facility. This money was utilised to repay project loans of £192.1 million provided by the European Investment Bank, £4.5 million interest and a £11.5 million penalty for early repayment.

On 16 March 2001 DCC made a further £300 million draw down under the Bridge Facility. This money was utilised to repay the £245 million debt due to Hyder plc and to fund working capital requirements.

On 30 April 2001 DCC made a further £75 million draw down under the Bridge Facility. This money was utilised to repay the final amounts owing and accrued interest under the finance lease provided by Capital Bank Leasing 3 Limited.

Total shareholder funds were reduced by £452.6 million to £742.7 million and indebtedness increased to £1432.6 million.

(2) Unsecured amounts falling due within one year include the bank overdraft balance of £28.8 million This overdraft arises from treasury activities undertaken by Hyder on behalf of its subsidiaries and at any time is offset by money market cash deposits held by DCC, which at 31 December 2000 amounted to £29.8 million. As an independent company, the bank overdraft at 31 December 2000 would have been repaid by the redemption of the cash deposits. The money market deposits are held by financial institutions other than the provider of the bank overdraft, and the cash deposits and bank overdraft have been separately disclosed in the unaudited management accounts for the nine months ended 31 December 2000 (see Appendix E).

Ofwat's 1999 price determination

The November 1999 price determination was the culmination of a two and half year process, during which Ofwat consulted publicly on methodology, expenditure priorities, and draft price determinations for each Regulated Company. As in 1994, Ofwat based their price determinations on a "building block" approach. For each company a revenue requirement for each of the five years was principally derived as the sum of:

- operating expenditure;
- capital maintenance (comprising infrastructure renewals charge ("**IRC**") and current cost depreciation ("**CCD**")); and
- return on capital, in turn calculated as the cost of capital multiplied by the regulatory asset value.

Having regard to the fact that forecast revenue does not move precisely in line with K factors, (e.g. because of domestic metering and movements in numbers of customers and metered demand) forecast revenues on a K = 0 basis were then used to translate the movement in annual revenue requirement into K factors.

Ofwat also prepared financial forecasts for the appointed business in order to ensure that proposed K factors would deliver financial ratios consistent with "solid investment grade ratings".

In preparing expenditure forecasts for each company, extensive use was made by Ofwat of comparisons between companies' own cost estimates, and a range of adjustments to company figures were accordingly made. A detailed account of Ofwat's approach to each "building block" is set out in "Future Water and Sewerage Charges 2000-05" (Ofwat November 1999).

Ofwat's estimate of the real weighted average cost of capital was derived using a Capital Asset Pricing Model Framework, with company-specific adjustments for the embedded debt premium.

Actual allowed returns, going forward, were higher still for several companies, including DCC (see below), reflecting two additional factors. First, in order to preserve efficiency incentives for operating expenditure so-called "incentive allowances" were added to the revenue requirement for the first three years reflecting out-performance of operating expenditure assumptions at the last periodic review. Second, those companies which voluntarily gave rebates to customers during the period 1995 to 2000 were given allowances to enable them to recover an equivalent amount over the next five years.

The methodology for calculating regulatory asset value for each company was established at the 1994 periodic review. Based initially on a measure of the value placed on the company's capital and debt by the financial markets following privatisation, it is essentially "rolled forward" to take account of projected new capital expenditure, (i.e. net of infrastructure renewals charges and current cost depreciation) and inflation.

At each of the two periodic reviews so far, projected regulatory asset values have been calculated initially on the basis of Ofwat's assumptions for capital expenditure going forwards. In 1999, Ofwat adopted a "rolling adjustment mechanism", under which capital efficiencies (the extent to which companies under-spend on their capital programmes as compared with Ofwat's original assumption) lead to a downward adjustment to the regulatory asset value, but with a five year lag.

Similarly, where a company had spent more than was assumed in the previous period, and the additional expenditure was associated with a new legal obligation, or where customers were demonstrably willing to pay for schemes to improve service standards, an upward adjustment to RAV would be made. Unlike capital efficiencies, such upward adjustments are not subject to a "rolling adjustment mechanism".

The assumptions on which Ofwat determined the price limits for DCC are set out in the following table.

		2000-01	2001-02	2002-03	2003-04	2004-05
Price limits (K)	%	(10.5)	(0.5)	0.0	1.2	1.0
Revenue	£m	428.8	424.5	423.6	427.9	431.4
Operating expenditure	£m	193.1	188.2	181.6	175.1	167.7
Current cost depreciation	£m	68.3	71.1	70.2	72.2	76.3
Infrastructure renewals charge	£m	31.5	31.2	31.0	30.7	30.4
Current cost operating profit	£m	137.1	135.0	141.5	150.7	157.5
Regulatory asset value (yr average)	£m	1,881.6	1,979.7	2,080.2	2,234.5	2,364.7
Post tax return on capital	%	7.1	6.6	6.6	6.4	6.2

Source: Ofwat Supplementary report for Dŵr Cymru, Table 6. All figures in May 1999 prices. The above table does not disclose the current cost working capital adjustment which ranges from £1.2 million in 2000/2001 to £0.5 million in 2004/2005.

DCC did not exercise its option to have Ofwat's determination referred to the CC.

Ofwat's 2000 Interim Determination

As set out in Chapter 8 under "*Interim Determinations of K*" a possible Interim Determination of price limits in specified circumstances is set out in condition B of the Licence.

In September 2000, DCC submitted an application for an Interim Determination in respect of a number of items, including higher than expected rates of domestic metering and additional costs arising out of new and confirmed legal requirements relating to cryptosporidium monitoring. In December 2000, Ofwat determined that DCC's price limits for the remaining four years of the five year period should be revised as follows:

	2001-02	2002-03	2003-04	2004-05
November 1999 determination	(0.5)	0.0	1.2	1.0
Revised price limits	0.2	0.7	2.0	1.8
Cumulative difference	0.7	1.4	2.2	3.0

DCC did not exercise its option to have Ofwat's Interim Determination referred to the CC. For further information on Ofwat's methodology, see "*Ofwat Letter*" in Appendix B which contains, *inter alia*, an explanation of the DGWS's approach to periodic reviews.

ILLUSTRATIVE FINANCIAL PROJECTIONS OF DCC

The table below sets out the illustrative financial projections of cash flows, net debt, regulatory asset values and certain ratios of DCC over the four years up to the next periodic review (the "**projections**"), which is considered to be a reasonable period of time. The projections have been prepared by DCC on the basis of present knowledge, fair estimates and assumptions (other than in the case of "Net Interest" below (which is provided purely for illustrative purposes)) which are believed by DCC to be reasonable. Ernst & Young have reviewed these projections, and their opinion thereon is attached as Appendix H. The projections do not constitute forecasts of the respective items, and no warranty or any other form of comfort is given by DCC or any other person as to the likelihood that the projections will prove to be reliable or accurate. The assumptions made for the purposes of preparing the projections are with respect to general business and economic conditions, other material contingencies and other matters not within the control of DCC or any other person and described in some detail below the table. These assumptions are inherently subject to significant uncertainties and their outcome cannot be predicted by DCC or any other person with any expectation of accuracy. Actual results are likely to differ, perhaps materially, from those projected due to a number of factors, including in particular the effect of those matters described in Chapter 5 "*Investment Considerations*". Accordingly, the projections are not necessarily indicative of future performance and have been prepared for inclusion in this Information Memorandum for illustrative purposes only.

Potential investors should regard the assumptions and projections with considerable caution and are urged to evaluate the potential for any assumption to deviate from those set out below and the implications of deviations in different assumptions on other assumptions and the revenues and the cash flows of DCC.

Illustrative Financial Projections

	Year Ending				
	Mar-01	Mar-02	Mar-03	Mar-04	Mar-05
	(All figures in £m)				
Income		**446**	**456**	**474**	**490**
Operating expenditure		(210)	(207)	(205)	(201)
Cash flow pre-capital maintenance		**236**	**249**	**269**	**289**
Capital maintenance expenditure		(87)	(88)	(89)	(90)
Cash flow post-capital maintenance		**149**	**161**	**180**	**199**
Net interest		(129)	(135)	(140)	(144)
Capital expenditure excluding capital maintenance		(180)	(159)	(126)	(185)
Rebates to customers		0	0	(11)	(12)
Pre financing net cashflow		**(160)**	**(133)**	**(97)**	**(142)**
Net debt (including indexation) (as at)	(1,856)	(2,028)	(2,173)	(2,284)	(2,443)
Regulatory Asset Value (RAV) (as at)	**1,989**	**2,201**	**2,397**	**2,562**	**2,783**
Ratios					
Senior interest cover pre-capital maintenance		2.44	2.42	2.50	2.57
Senior interest cover post-capital maintenance		1.53	1.56	1.67	1.77
Total net interest cover pre capital maintenance		1.83	1.85	1.93	2.01
Total net interest cover post capital maintenance		1.16	1.19	1.29	1.38
Total net debt to RAV (as at)	**93.3%**	**92.1%**	**90.6%**	**89.1%**	**87.8%**

Assumptions

The following are the assumptions used by DCC for the purpose of preparing the projections set out in the table above for the four year period from and including 1 April 2001 to and including 31 March 2005 (the "**Relevant Period**").

General Assumptions

Economic and business environment

It has been assumed that no material change will occur in the general economic and business environment during the Relevant Period.

Legislation

The projections have been prepared on the basis of principal legislative provisions relevant to DCC's activities currently in force, including in particular environmental and taxation legislation. It is assumed that no material changes in such legislation will occur during the Relevant Period.

Claims against DCC

It is assumed that no material claims, whether arising from principal legislative or contractual provisions, which may give rise to an entitlement to compensation, payment of fines or other penalties or charges, will arise during the Relevant Period.

Inflation

Where information extracted from Ofwat's Supplementary Report for DCC issued on 26 November 1999 has been used in the projections, published RPI inflation factors have been applied for the period where available, and thereafter inflation has been assumed at 2.5 per cent. per annum throughout the term of the Relevant Period. Specific provision is made in DCC's licence for determining the inflation factor to be applied to customer charges, in particular, inflation of 1.4 per cent. (being the movement in the RPI for the year ended November 1999) has been used for the year ended 31 March 2001 and 3.2 per cent. (being the movement in the RPI for the year ended November 2000) has been used for the year ended 31 March 2002.

Regulatory Asset Value

RAV at 31 March 2001 is based upon RAV at March 2000 as determined by the 1999 Price Review adjusted for projected capital expenditure and inflation, and estimated regulatory depreciation for the year ended 31 March 2001. Future RAV is based upon projected capital expenditure and inflation, and estimated regulatory depreciation. Estimated regulatory depreciation for the year to 31 March 2001 and throughout the Relevant Period has been based upon the 1999 Price Review Determination.

Accounting Policies

It has been assumed that the accounting policies applied by DCC in its audited accounts for the year ended 31 March 2000 will continue to be applied throughout the Relevant Period, save that the treatment of deferred taxation is assumed to follow the provisions of Financial Reporting Standard 19 – Deferred Tax for accounting periods commencing 1 April 2001 and thereafter.

Cash Flow

Income

Projected income is based upon reported turnover for the financial year ended 31 March 2000 adjusted to take account of:

- the effect on permitted prices of the 1999 Price Review and the 2000 Interim Determination; and
- specific volume assumptions in respect of the growth of the domestic customer base, metered water consumption, the numbers of customers switching from unmeasured to measured supply, and the estimated impact of planned plant closures by Corus plc in Wales (approximately £3 million per annum).

Appropriate price adjustments have been made to restate income to outturn price levels using the inflation factors described above.

Operating Costs

Operating cost projections have been derived from two elements:

- outsourced and own costs, which reflect the operating cost allowance determined by Ofwat at the 1999 Regulatory Review as subsequently modified by the 2000 Interim Determination ("**Base Operating Costs**"); and
- the principal terms of the CfD (see Chapter 12 under "***Contract for Differences***").

Appropriate price adjustments have been made to restate these items to outturn price levels using the inflation factors described above.

Outsourced operating costs are assumed to amount to 58 per cent. of the outturn Base Operating Costs, increased by a 5 per cent. allowance for operating cost margin as provided for in the CfD. It has been assumed that the outsourced services contracts will be on terms identical to that provided for in the CfD, and that DCC's outsourced operating costs will therefore be as determined by the CfD.

Own operating costs are assumed to amount to 42 per cent. of the outturn Base Operating Costs.

Capital Maintenance Expenditure

Capital maintenance expenditure comprises two elements: Infrastructure renewals charge and non-infrastructure capital maintenance. Both elements have been projected on the basis of the respective allowances given by Ofwat at the 1999 Price Review. Appropriate price adjustments have been made to restate these items to outturn price levels using the inflation factors described above.

Net Interest

As referred to above, net interest has been provided purely for illustrative purposes on the following basis:

- Interest payable under the Initial Intercompany Loan Agreement has been assumed at a weighted average interest rate of 7.08 per cent. (including indexation of Indexed Bonds), and on subsequent borrowings is assumed to be at a weighted average interest rate of 6.88 per cent.;
- Interest receivable on cash balances is assumed to be at a rate of 5 per cent.; and
- Interest on Finance Leases and Local Authority Loans has been projected on the basis of their respective terms and the Gen Re Swap is assumed to continue throughout the Relevant Period.

Interest has been calculated on the average borrowing or cash balance outstanding during a financial year. It is assumed that interest revenue is received in the year it is earned, and that interest expense (other than indexation of Indexed Bonds) is paid in the year it is charged.

No account has been taken of any interest receivable by DCC under the Holdings/DCC Loan Agreement as it constitutes non-third party interest income which arises solely within the Glas Group and is matched by an equal interest expense in Holdings.

Customer Rebates

These assumptions have been prepared and provided by Glas, are its sole responsibility, and Glas believes them to be based on fair estimates. Rebates are discretionary and may only be made if certain financial conditions are satisfied (see Chapter 4 under ''*Common Terms Agreement – DCC Covenants*'').

Capital Expenditure excluding maintenance

Capital expenditure excluding maintenance has been projected on the basis of the allowances given by Ofwat at the 1999 Price Review, supplemented by a further capital expenditure allowance arising from the 2000 Interim Determination. Appropriate price adjustments have been made to restate these items to outturn price levels using the inflation factors described above.

Taxation

It is projected that no corporation tax will be payable during the relevant period.

Working capital

Working capital, comprising stocks, debtors and creditors (including both revenue and capital items, but excluding all financing debtors and creditors) is assumed to remain unchanged throughout the period at the estimated working capital level at 31 March 2001.

BBV LETTER

Binnie Black & Veatch Ltd

4 May 2001

Citibank, N.A.
Citigroup Centre
33 Canada Square
5th Floor, Canary Wharf
London E14 5LB

The Royal Bank of Scotland plc
135 Bishopsgate
London EC2M 3UR

MBIA Assurance S.A.
London Branch
1 Great St Helen's
2nd Floor
London EC3A 6HX

Dŵr Cymru Cyfyngedig
Plas y Ffynnon
Cambrian Way
Brecon, Powys
Wales LD3 7HP

Dear Sirs

We write in connection with the multicurrency programme for the issuance by Dwr Cymru (Financing) Limited of up to £3,000,000,000 Guaranteed Asset-Backed Bonds, and up to £3,000,000,000 Asset-Backed Bonds, including up to £200,000,000 Class R Asset-Backed Bonds financing Dŵr Cymru Cyfyngedig (''DCC'').

This letter draws together the findings and conclusions of a technical study covering the operations of DCC. The study has focused on identifying technical risks and how those risks are mitigated under the contractual and financial structure.

The findings and conclusions in this letter reflect the professional judgement of Binnie Black & Veatch Ltd (BB&V) based upon the information made available to it. BB&V has relied on, and not independently verified, such information. A number of assumptions have been made during the course of the analysis. While BB&V has no reason to believe that these assumptions are unreasonable, it is noted that if any prove incorrect, actual results could vary from those projected.

We have based the study on:

- An assessment of DCC's submissions to Ofwat and the Reporter's comments on the submissions, together with discussions with the Reporter.
- Ofwat's ''Final Determination: Future Water Supply and Sewerage Charges 2000-5 – Supplementary Report for Hyder Ltd.''
- Detailed meetings and contacts with DCC management and other investigations carried out during the study.

We conclude as follows:

- Following a full and detailed review of the DCC assets undertaken by others in 1998, and having taken note of asset improvements since then, we consider the asset condition to be predominantly sound. Such deterioration, as may occur during the period 2000/5, should not have a significant effect on customers.
- DCC has taken management action to procure its capital programme for the AMP3 period (2000 – 2005) by forming alliances with a select group of contractors. The proposals are sensible, and the concept of an alliance is a positive way to control and drive down costs. DCC used a similar approach to make savings against its previous AMP2 (1995 – 2000)

budget. DCC are already starting to demonstrate cost savings on their AMP3 capital budgets. From our studies we conclude that there is only a very low probability of DCC exceeding their capital budget.

- DCC's main concern is its operating costs and the continuing efficiencies that it will have to make. It believes that it will minimise its exposure by pursuing an outsourcing strategy via operations and operational maintenance, and customer services contracts. In addition, DCC's operational and customer service costs under the outsourcing strategy are fixed at a certain level until 31 March 2005 under an agreement with WPD Finance Limited. Therefore, from DCC's viewpoint there are no significant risks remaining in its operational budgets.
- Based on the foregoing, we consider that DCC should be able to operate within the Ofwat price determination, without taking undue risks with compliance or levels of service. DCC has a sound management structure in place and appears to operate in line with water industry best practice.
- DCC face a number of environmental risks, including contamination of water supplies, chemical discharges, pollution of sources of supply, and discharges of effluents and sludges from water and wastewater treatment works. We consider that risk levels will generally be low and DCC have appropriate mitigation measures and emergency plans in place to prevent disruption of supplies of adequate quality to customers and any serious environmental impacts.
- DCC may seek an 'Interim Determination', which may arise from a matter notified by the Regulator, or a change in legal obligations. Such an 'Interim Determination' is subject to a materiality threshold. For DCC the materiality limit is effectively at 1 per cent. of turnover.

During the study BB&V reviewed the technical risks and mitigating factors associated with all the above elements. We are satisfied that the identified risks are mitigated through the means of delivery or by insurance measures and the regulatory regime.

Any reliance on this letter by a third party or decision therefrom by a third party is the sole responsibility of such third party. BB&V shall not accept, and does not owe, any duty of care to any third parties relying on this letter and shall have no financial or other liability to any such party with respect to any matter related to decisions made by any such party based in whole or in part on this letter.

Yours faithfully

W THOMSON
Project Director

CHAPTER 10

RELEVANT TRANSFER AGREEMENTS

HUH

HUH was incorporated in England and Wales on 18 July 1997 as a limited company under the Companies Act, with registered number 3405267. HUH's authorised capital is £1,120,067,997 divided into 1,120,067,997 ordinary shares of £1 each. 1,120,067,997 such ordinary shares have been issued which are fully paid-up. Hyder holds 1,120,067,996 ordinary shares and a share trustee holds one ordinary share on trust for Hyder.

HUH's registered office is at PO Box 295, Alexandra Gate, Rover Way, Cardiff, CF24 5UE and its secretary is Mrs. Sally Jones. HUH's directors are Dr. Michael Peter Brooker, Mr. Daniel Charl Stephanus Oosthuizen and Mr. Robert Arthur Symons (see Chapter 9 under "*DCC Directors and Secretary*" for further details) and their business address is PO Box 295, Alexandra Gate, Rover Way, Cardiff CF24 5UE.

HUH's auditors are PricewaterhouseCoopers, chartered accountants. Statutory accounts have been prepared and delivered to the Register of Companies in England and Wales since HUH's incorporation. The last such accounts were made up to 31 March 2000.

SHARE PURCHASE AGREEMENT

On 5 February, 2001, HUH entered into the Share Purchase Agreement with Glas Securities under which HUH will sell the entire issued share capital (other than the redeemable preferred ordinary shares already owned by Glas Securities) of Holdings to Glas Securities. As at the date of this Information Memorandum, the sale is conditional, *inter alia*, on the issue of the first Series of Bonds by the Issuer on the Initial Issue Date.

Pursuant to the Share Purchase Agreement, WPDH unconditionally and irrevocably guarantees to Glas and Glas Securities the due and complete performance by HUH of its obligations thereunder, and Glas unconditionally and irrevocably guarantees to HUH and WPDH the due and complete performance of Glas Securities' obligations thereunder.

The consideration for the acquisition is £1 on the basis that the Financing Group will have debt and cash ("**Net Debt**") in a net amount of £1,850 million (such figure will also be adjusted upwards to take account of reimbursements of fees and expenses due to WPDL) at completion of the Share Purchase Agreement.

Prior to completion of the Share Purchase Agreement a dividend will be declared by DCC in an amount estimated to result in the amount of Net Debt upon completion being at the requisite level. This dividend will be paid by DCC at completion of the Share Purchase Agreement to HUH (HUH having retained the rights, on the transfer of all the ordinary shares in DCC, to all dividends declared or made by DCC prior to completion of the Share Purchase Agreement). In addition, Glas Securities shall procure that Holdings makes a payment to HUH, or, if applicable, HUH will make such a payment to Holdings, to adjust the consideration paid by Holdings for the DCC shares under the share purchase agreement between Holdings and HUH and HSU for the DCC Shares. This adjusting payment will be based on the working capital and net capital expenditure figures for DCC at the completion of the Share Purchase Agreement.

Warranties have been given by HUH as to corporate, financial, legal, employment, pensions and tax matters. A tax covenant will also be entered into on completion of the Share Purchase Agreement. The total aggregate liability of HUH for breach of the warranties under the Share Purchase Agreement or under the tax covenant is £50 million. The time limit for bringing claims under the general warranties is 18 months from completion of the Share Purchase Agreement and seven years from completion in respect of tax warranty claims and claims under the tax covenant. The ability of Glas Securities to make claims under the warranties and the tax covenant is also subject to certain other limitations.

It is possible for Glas Securities to rescind the Share Purchase Agreement in the period between signing and completion if there is a breach of the warranties which would entitle Glas Securities to a claim having a value in excess of £50 million and such breach is not remedied by HUH to the extent that the value of the claim would then be less than £50 million.

ASSET SALE AGREEMENT

DCC entered into an agreement (the "**Asset Sale Agreement**") with Hyder Industrial Group Limited ("**HIG**") on 23 February 2001 pursuant to which DCC will sell to HIG certain freehold and leasehold properties currently owned by DCC, including houses, farms, offices, depots, radio sites, surplus operational properties and sub-station sites (the "**Properties**" and each a "**Property**").

Price

The price for each of the Properties will be the price approved by the DGWS plus VAT, where appropriate. HIG has paid to DCC an estimated price of £19,512,055 for all of the Properties (the "**Estimated Purchase Price**"). VAT will be payable on completion of the sale of certain of the Properties.

If the price approved by the DGWS is more than the Estimated Purchase Price, HIG will on completion pay the difference to DCC. If the price approved by the DGWS is less than the Estimated Purchase Price, then on completion DCC will pay the difference to HIG together with accrued interest or other sum earned on that amount in the hands of DCC ("**Interest Accrued**").

Completion

Completion of the sale of each Property may take place independently of the completion of the sale of any other Property. Completion is conditional on and will take place on or before 10 working days after the later of the DGWS confirming his approval or consent of the transfer of the Properties, the completion of the sale by HUH of the shares in DCC or any holding or parent company of DCC, including Holdings, pursuant to the Share Purchase Agreement, HIG confirming by notice in writing to DCC that it is satisfied with, *inter alia*, the title deduced and all necessary consents of the DGWS, the EA (in relation to certain specified properties) and landlords (in relation to any leasehold Property) having been obtained.

Leasebacks

HIG will leaseback to DCC those parts of the Properties which are used for the purpose of DCC's business. The leases will have a term of 20 years with a tenant's break right after 5 years. The rents are to be agreed between DCC and HIG but in the event of disagreement, shall be determined by independent surveyors.

Clawback

The DGWS may stipulate as part of his consent that DCC or members of DCC's group share in any part of any future uplift in value triggered by an enhancement in value, disposal, or anything similar to those concepts ("**Clawback**"). If so, appropriate provisions will be included in the relevant transfer of each Property.

Environmental Matters

DCC will remain liable for and indemnify HIG against all liability in relation to any contamination present at or migrating from any Property at any time before completion of the transfer of that Property, up to a maximum liability of £10 million. If the costs and expenses of removing, containing and/or treating such contamination are greater than the open market value of the Property (disregarding contamination), DCC may either buy back the Property (at open market value disregarding any contamination) or pay the remediation costs.

HIG will be liable for and indemnify DCC against all liability incurred by DCC in excess of £10 million (and HIG will only be liable for that excess) in relation to any contamination present at or migrating from any Property on or before completion of the transfer of that Property.

Assignment

Apart from one party assigning its rights or benefits to a member of its own group, DCC is permitted to grant a fixed charge over its rights and benefits under the Asset Sale Agreement by way of an assignment by way of security and HIG is entitled to assign to a purchaser of the shares in DCC or any holding or parent company of DCC, including Holdings.

Right to Rescind and Termination

(a) HIG has the right to rescind the Asset Sale Agreement (in relation to relevant Properties) by notice in writing to DCC including if (i) the sale by HUH of the shares in DCC, or any holding or parent company, including Holdings, is not completed within 6 months from the date of the Asset Sale Agreement; or (ii) approval or consent from the DGWS in relation to the sale of the Properties has not been given within 6 months from the date of the Asset Sale Agreement; (iii) DCC's board do not approve the terms of the Asset Sale Agreement at DCC's board meeting on 12 March 2001 or any adjournment thereof; or (iv) the DGWS determines Clawback is necessary or if he has not agreed the terms of any such Clawback in any transfer of that Property within 6 months from the date of the Asset Sale Agreement. There are additional rights for HIG to rescind in relation to certain Properties if certain conditions specific to the relevant Property are not met.

(b) HIG also has the right to rescind the Asset Sale Agreement in relation to all or any of the Properties by notice in writing to DCC if HIG is dissatisfied with, *inter alia*, encumbrances deduced or following inspection of the Properties.

(c) If the conditions in (a) have not been satisfied within 2 years from the date of the Asset Sale Agreement then, subject to certain conditions, DCC will have the right to terminate the Asset Sale Agreement by notice in writing to HIG within the following 12 month period. In any event, if the conditions in (a) have not been satisfied and such 12 month period has expired DCC has the right to serve notice to terminate.

If notice is given pursuant to (a), (b) or (c) above and the Asset Sale Agreement no longer applies in relation to all of the Properties, DCC must procure with immediate effect repayment of the Estimated Purchase Price in full, together with the amount of Interest Accrued. If the notice served relates to some only of the Properties then DCC must repay in full to HIG the part of the Estimated Purchase Price which is attributable to the particular Properties together with the amount of Interest Accrued.

Approval of the Asset Sale Agreement is required from the DGWS. This is currently being sought by DCC.

HOLDINGS/DCC LOAN AGREEMENT

DCC has entered into an agreement with Holdings pursuant to which DCC will make advances to Holdings (the "**Holdings/DCC Loan Agreement**") in an aggregate amount not exceeding £459 million (the "**Loan Amount**"). The loan is to be made to enable Holdings to pay the cash consideration payable by Holdings to HUH and HSU as consideration for the acquisition by Holdings from HUH of all the issued ordinary shares in DCC and from HSU of all the preference shares in DCC under the share purchase agreement dated 22 March 2001 between HUH, HSU and Holdings.

The obligation of DCC to make any advances to Holdings will be subject to, amongst other things, the receipt of funds by DCC from the Issuer under the Intercompany Loan Agreement sufficient to fund the advance of the Loan Amount under the Holdings/DCC Loan Agreement and the approval of the DGWS of the Loan Amount.

Any amount payable by DCC to Holdings may be set off by DCC against the Loan Amount, any deferred interest, any deferred increased costs or any accrued interest or fee payable under the Holdings/DCC Loan Agreement.

Interest

The interest on the Loan Amount is 12 per cent. and will accrue daily. The first interest payment will be due on 30 September 2001, and thereafter interest is payable semi-annually. Holdings may, on written notice to DCC, defer any interest payment in which case interest will be payable on the deferred interest as if it were a separate loan.

Repayment

The Loan Amount will be repayable in full (including all accrued interest, deferred interest, deferred increased costs and other fees and charges ("**other amounts**") on the later to occur of (i) 31 March 2035 and (ii) the date which is two years and one day after the final maturity date of the longest-dated Bond issued from time to time by the Issuer.

The term for repayment of the Loan Amount may be extended at the mutual agreement of the parties for a term nominated by Holdings. Unless otherwise agreed, the period of the extension will be governed by the terms set out in the Holdings/DCC Loan Agreement. Holdings is permitted to make a pre-payment of the Loan Amount subject to payment of any break costs incurred by DCC.

Termination

DCC may terminate the Holdings/DCC Loan Agreement immediately by written notice if any of the following events of default occur:

(a) non-payment by Holdings under the Holdings/DCC Loan Agreement;

(b) an insolvency event occurs in respect of Holdings;

(c) it becomes illegal for Holdings to comply with any of its obligations under the Holdings/DCC Loan Agreement;

(d) Holdings breaches any of its undertakings under the Holdings/DCC Loan Agreement; or

(e) notice is served on DCC pursuant to the Initial Intercompany Loan Agreement declaring all or any part of the Advances (as defined therein) to be immediately due and payable.

The Loan Amount outstanding (as well as other amounts) will become immediately repayable upon such termination. Default interest at the rate of 1 per cent. above the interest rate will be paid on any overdue sum payable .

Undertakings

DCC undertakes to do all that is necessary and within its power to secure receipt of funds under the Intercompany Loan Agreement. Holdings provides undertakings with respect to security interests, transfers and creation of equitable interests over its assets, carrying on its business, incurring indebtedness, merger and employees.

Increased costs

Holdings will be required to compensate DCC for increased costs but this may be deferred. Interest will be payable on any such deferred amount as if it were a separate loan under the Holdings/ DCC Loan Agreement.

Assignment

DCC may transfer or assign all or any of its rights under the Holdings/DCC Loan Agreement.

CHAPTER 11

GLAS CYMRU CYFYNGEDIG

INCORPORATION, BOARD OF DIRECTORS AND MANAGEMENT

Glas is a private company limited by guarantee. Glas was incorporated in England and Wales on 13 April 2000 under the Companies Act, with registered number 03975719. It was established for the purpose of acquiring and owning DCC.

On 3 November 2000, Glas announced that it had reached agreement with WPDL on terms for Glas to acquire DCC from WPDL. A contract for the sale and purchase of Holdings, DCC, WWUF and the Issuer was entered into on 5 February 2001 between, *inter alios*, Glas Securities and HUH (see Chapter 10 under "*Share Purchase Agreement*").

The registered office of Glas is 1 Kingsway, Cardiff CF10 3PW.

The Chairman of the board of Glas is Lord Burns, former Permanent Secretary to the Treasury and currently non-executive director of Legal & General plc, Pearson plc and British Land plc. Lord Burns has recently been appointed Chairman of the National Lottery Commission.

The other non-executive directors are set out below:

Mr. Geraint Talfan Davies

Former Controller of BBC Wales and current Chairman of the Institute of Welsh Affairs. Recently appointed by the Department of Culture, Media and Sport as the first member of the Radio Authority with special responsibility to cover Wales.

Mrs. Alison Carnwath

Chairman of Vitec Group plc and a non-executive director of the Nationwide Building Society, Man Group plc, Arcadia Group PLC and Skillsgroup plc .

Mr. Anthony Hobson

Former Group Finance Director of Legal & General Group plc and former non-executive director of Thames Water plc.

Dame Deirdre Hine

Former Chief Medical Officer at the Welsh Office and member of the Audit Commission for England and Wales and current President of the Royal Society of Medicine, Chairman of the Commission for Health Improvement and Independent Member of the House of Lords Appointments Commission.

Mr. John Bryant

Former Joint Chief Executive of Corus plc and currently a non-executive director of the Bank of Wales.

The two executive directors of Glas are Mr. Nigel Annett and Mr. Christopher Jones who until 3 November 2000 were directors of DCC. Dr. Michael Brooker, Managing Director of DCC, will join the Board of Glas upon the completion of the acquisition of DCC by Glas Securities. Glas's company secretary is Mr. Richard Curtis. The business address of each of the non-executive and executive directors is the registered office of Glas.

The auditors of Glas will be PricewaterhouseCoopers, chartered accountants. No statutory accounts have been prepared since the incorporation of Glas. Its first statutory accounts will be drawn at and to 31 March 2001 and its accounting reference date will be 31 March of each year.

CORPORATE GOVERNANCE

The constitution of Glas limits its purposes to that of acting as a holding company and ensuring the proper carrying out of DCC's functions and responsibilities in accordance with the Licence and applicable law and regulation. One of Ofwat's proposed licence modifications is that Glas gives an undertaking to DCC prohibiting Glas and its subsidiaries from making any changes to their Memorandum and Articles of Association (the "**Articles**") without the DGWS's consent.

The Board of Glas is accountable to the members of Glas. Glas currently has 8 members and intends to appoint up to 50 members in 2001. Members will not be entitled to receive dividends and, other than their liability to pay £1 upon a winding up of the company, have no financial interest in the company. Members will be individuals from across the region currently served by DCC with backgrounds in a variety of sectors including industry, commerce, finance, small business, education, health, the environment, charities and local government.

The Articles also require that the Board be composed of a majority of non-executive directors. In addition one of Ofwat's proposed licence modifications (see ''*Proposed Modifications*'' below) requires the board of Glas to have at all times a majority of independent non-executive directors.

The Articles also require the Board to ensure that at all times there is a published written policy setting out procedures for seeking nominations for membership and for the selection and appointment of members (the ''**Membership Policy**''). The Membership Policy was published on 12 March 2001. Members are put forward by an independent panel in accordance with the Membership Policy which is largely based on the ''Nolan'' principles as set out in the Nolan Committee – First Report of the Committee on Standards in Public Life (May 1995). The panel consists of one non-executive Director of Glas and a number of independent appointees, including the chairman, Ms Janet Lewis Jones. She was previously a senior official in the Home Office and served in both the Cabinet Office and the Privy Council. She was involved in the privatisation of the water companies in 1989 and has had roles with S4C, the British Board of Film Classification and the Equal Opportunities Commission.

Under Glas's Articles, every member shall be bound to exercise his rights and powers as a member to further the objects of the company as set out in Glas's Memorandum of Association. It is intended that they will play a key role in providing a critical oversight and holding the Board to account for the performance of Glas. They will be assisted in this task by quarterly reports, half-yearly statements of performance, an annual report and an annual general meeting which will include presentations on the company's general and financial performance and on its customer service, water quality and environmental performance. The members have the usual Companies Act rights to remove directors and to elect their replacements.

The board of DCC will be required by one of the proposed licence modifications to act in accordance with the Principles of Good Governance and Code of Best Practice as appended to the listing rules of the UK Listing Authority (the ''**Combined Code**''). Glas is also subject to the provisions of the UK Companies Acts 1985 and 1989. In addition, Glas intends to operate as if it were a publicly listed company in all material respects as regards corporate governance and reporting.

INCENTIVES FOR PERFORMANCE

The Board of Glas intends to implement a remuneration policy for executive directors which will create incentives to deliver benefits for creditors and customers. The Remuneration Committee of the Board has prepared a policy which seeks to achieve the following objectives:

- to reward management for improvements in credit quality, financial strength, and the consequent delivery of reductions in bills for customers; and
- to reward management for service performance, both in terms of level and rate of improvement, in comparison with the rest of the industry.

Under the policy executive directors will be eligible for bonuses of a percentage of base salary. A substantial portion of payable bonuses will be deferred for three years and executive directors will forfeit their deferred bonus if their employment is terminated. In this way it is intended that executive directors will have incentives to ''lock in'' to Glas for the longer term. Approximately half of annual bonus will be based on financial performance and the remainder will be based on service performance.

Financial performance will be measured with reference to the annual growth in the ''economic reserve'', defined as the RAV less net debt, adjusted upwards in respect of customer rebates paid in the year. Executive directors will be incentivised to deliver significant reductions each year in the RAR. In addition, there will be adjustments to reflect movements in the credit ratings of each Class of Bonds. It is intended that incentives to deliver financial results will provide creditors with ongoing improvements in credit quality.

Service performance will be measured with reference to the overall service assessment rankings published by Ofwat each year. These take account of water quality, environmental performance, and customer service. The proportion of maximum bonus payable will depend upon the ranking of DCC compared to the other Regulated Companies, adjusted by a factor which reflects any movement in ranking since the previous year (subject to a maximum of 100 per cent. and a minimum of zero).

Finally, the management of DCC will continue to be subject to a range of external disciplines and pressures. The company will continue to operate within the same strict legal and regulatory framework as other Regulated Companies. It will also be subject to monitoring by the Beneficiary Instructing Group.

GLAS SECURITIES

Glas Securities was incorporated in England and Wales on 21 December 2000 as a private limited company under the Companies Act, with registered number 4129132. Upon incorporation, Glas Securities was named Hackremco (No. 1771) Limited but subsequently changed its name to Glas Cymru (Securities) Cyfyngedig on 1 February 2001.

Glas Securities' authorised share capital is £100 divided into 100 ordinary shares of £1 each. One such ordinary share has been issued and is fully paid-up and held by Glas. As at the date of this Information Memorandum, Glas Securities has no other equity or debt capital.

The registered office of Glas Securities' is at 1 Kingsway, Cardiff, CF10 3PW and its secretary is Mr. Richard Curtis. The directors of Glas Securities are Mr. Christopher Jones, Mr. Nigel Annett, Lord Burns, Mr. Geraint Talfan Davies, Mrs. Alison Carnwath, Mr. Anthony Hobson, Dame Deidre Hine and Mr. John Bryant. For further details of the directors of Glas Securities, all of whom are also directors of Glas, see ''*Incorporation, Board of Directors and Management*'' above.

The auditors of Glas Securities will be PricewaterhouseCoopers, chartered accountants. No statutory accounts have been prepared since the incorporation of Glas Securities. Its first statutory accounts will be drawn at and to 31 March 2002, and its accounting reference date will be 31 March of each year.

GLAS AND THE REGULATOR

The Policy of the Regulator to Ownership Structures in the Water Industry

On 6 June 2000 Ofwat published a consultation paper on ''New Ownership Structures in the Water Industry'' (the ''**New Ownership Structures Paper**'') which addressed the constitutional and regulatory issues arising from the separation of the ownership of a water company's assets (and the licence) from the operations of those assets. The paper considered the introduction of new forms of corporate structure and ownership for appointed businesses, including mutual trusts and not-for-profit companies limited by guarantee. The then DGWS invited views on the following issues: (i) restructuring and incentives for efficiency; (ii) constitutional arrangements; (iii) procurement of services; (iv) competition; and (v) finance and risk.

On 20 June 2000 Ofwat published a further consultation paper on ''The proposed restructuring of the Kelda Group''. This considered the issues arising from a proposed restructuring which would separate asset ownership from operations and create a customer-owned body which would acquire the shares and assets of the Regulated Company (the ''**Kelda Proposals**''). The proposed asset owning company would be 100 per cent. debt financed. The then DGWS referred to the ''New Ownership Structures Paper'' and the five issues raised by it in as far as they were relevant to the Kelda Proposals.

The then DGWS issued his preliminary assessment on ''The Proposed Restructuring of the Kelda Group'' on 25 July 2000 (the ''**Kelda Assessment**''). He did not approve the scheme but said that whilst he had no objection in principle to the separation of asset ownership from operations and procurement of services (because of the potential for greater efficiency from the introduction of increased competition) he felt that benefits to customers were not sufficiently demonstrated by the proposals and that practical concerns had not been adequately addressed.

The DGWS said that any revised proposals should, amongst other things: (i) satisfy practical concerns regarding water quality and the environment, (ii) ensure the independence of the asset-owner from the existing licence holder, (iii) demonstrate benefits to customers, (iv) establish the provision of incentives for efficiency and (v) involve customers in a period of consultation. As a

minimum he would require licence amendments dealing with the constitution of the new asset-owner, its accountability, the procurement plan, control over statutory and licence obligations and the independence of the asset-owner.

Glas and the Regulator

On 3 November 2000, Glas announced that it had reached agreement with WPD to acquire DCC subject to contract and also to regulatory and other approvals. On the same day Glas issued a public document setting out its proposals for DCC and Lord Burns sent an open letter to the DGWS on behalf of the board of directors of Glas (the "**Open Letter**"). This letter set out the ways in which the Glas proposals addressed the regulatory concerns raised in the Kelda Assessment particularly in relation to independence and the board, corporate governance and incentives, acceptability to customers and consultation, benefits to customers and continuity of water and wastewater services.

An Ofwat consultation paper "The proposed acquisition of Dŵr Cymru Cyfyngedig by Glas Cymru Cyfyngedig" was published on 10 November 2000 and this set out the issues raised by the proposed acquisition and mentioned in the Open Letter. The paper set out proposed licence modifications and sought comments on whether or not these were adequate to protect customers' interests. In setting down some of the background to the proposals Ofwat distinguished them from the Kelda Proposals in that the vehicle of ownership proposed was a company limited by guarantee and customers would not become owners of the regulated business.

Ofwat invited views by 18 December 2000 on benefits and risks for customers, customer consultation, change of ownership, incentives for efficiency, constitutional arrangements, procurement of services, comparative information and additional licence modifications sought by Glas. Key questions raised in the consultation were (i) whether a debt-financed structure would be as resilient as shareholder-owned equity-financed water companies, (ii) whether the absence of shareholders would effect incentives for efficiency and (iii) whether the outsourcing of operations would leave DCC without proper control over its functions. Ofwat reviewed the proposals as they related to the framework set out in the Kelda Assessment.

Following this consultation period Ofwat published a position paper (the "**Position Paper**") on the Glas proposals on 31 January 2001 in which the DGWS concluded that it did not object to Glas's proposals and that Glas should be allowed to proceed to test whether it could secure the financing. The DGWS concluded that Ofwat should not object to the proposals provided that Glas:

- agreed to the proposed licence modifications (see below);
- gave a public commitment to customer benefits;
- made public its incentive schemes for executive management;
- provided a public statement on its commitment to limiting its activities to the single purpose of providing water and sewerage services;
- gave a public commitment to appointing the members of Glas on the basis of best practice; and
- confirmed that the rights proposed for bondholders did not impede the DGWS's duties under the WIA.

As a Regulated Company, DCC would continue to be subject to regulation on the same basis as other companies including the setting of price limits by reference to sector comparatives. Ofwat noted that the consultation had shown broad support in Wales for Glas, notably from the Assembly (see "*The Assembly and Glas*" below) and also from the CSC for Wales. Finally, the DGWS distinguished the Glas proposals from other attempts at restructuring on the basis of the support of the Assembly, the wish of WPD not to continue its involvement in the water sector, the discount in the purchase price relative to the RAV and the clear independence of Glas from WPD.

The Position Paper made, *inter alia*, the following assessment:

Financing plan

- While Glas's structured debt approach is a new form of financing for a Regulated Company and therefore carries an element of risk, the elimination of risk from diversification into non-regulated activities is significant in terms of securing financing and Ofwat has proposed a new licence condition to secure this.
- Glas has secured commitments from its financiers, including MBIA.
- Provision of implicit reserves in terms of borrowing capacity is ensured by the discount to RCV in the purchase price.
- There is potential for significant savings in financing costs.

Incentives for efficiency

- Although Ofwat believes that these incentives are unlikely to be as strong as under shareholder ownership Glas has sought to build in mechanisms to mitigate this.
- These include (i) linking executive management remuneration to performance, (ii) an undertaking from Glas that it will maintain a majority of non-executive directors (iii) the public statement on customer rebates and (iv) the involvement of the Financial Guarantors in monitoring performance to provide external commercial pressure.

Control of operations

- Outsourcing must not lead to a blurring of responsibility for safety and environmental outputs.
- A proposed licence modification will ensure that DCC retains its responsibilities to the DWI and the EA.
- Success will depend on the existence of a proper market and on the quality of the Glas management.
- Ofwat attaches particular importance to the fact that operations and customer service contracts will be competitively tendered from the outset.
- A proposed new licence condition requires that Glas provide information on contractors' costs to Ofwat to facilitate cost comparisons.

Independence from the current owner

- Ofwat is satisfied that Glas is independent of WPD.
- The Board is led by independent non-executive directors.

Membership

- Ofwat expects Glas to conduct its recruitment process in line with codes of best practice.
- Since members will have the power to direct board policies, Ofwat has proposed a new licence condition requiring DCC to obtain an undertaking from Glas prohibiting it from making changes to its Memorandum and Articles of Association without Ofwat's consent.

Proposed Modifications

Appendix B to the Position Paper summarises the licence modifications proposed by the DGWS. Glas and WPDL have agreed to these licence modifications (as set out below) which include the licence modifications agreed in principle by WPDL upon its acquisition of Hyder. On 7 March 2001 the DGWS formally published a description of the proposed modifications and requested that any objections or representations be submitted by 4 April 2001. As at the date of this Information Memorandum, Ofwat has still to confirm implementation of the proposed modifications. The Assembly has confirmed in a letter to Glas dated 16 March 2001 that it will not exercise its power to block the proposed modifications.

1. *DCC's responsibilities as a water and a sewerage undertaker*

DCC's Licence already requires that its Board of directors certify annually to the DGWS the adequacy of its financial and management resources, to enable it to discharge its core functions for the ensuing year. The DGWS proposes that these requirements be extended to require that DCC's Board will certify annually the sufficiency of its methods of planning and control, to enable it to discharge its functions for the ensuing year.

For these purposes, DCC will be required to ensure that those systems for planning and internal control comply with requirements specified by the DGWS in written, published guidance. This will ensure that DCC maintains proper control over its legal obligations and responsibilities as a water and sewerage undertaker and also that it pursues proper market-testing of whatever services it chooses to continue to outsource (see Section 2 below).

The guidance on internal planning and control is based upon the Combined Code of the Committee on Corporate Governance and on the Turnbull Report: Internal Control – Guidance for Directors on the Combined Code (September 1999).

They require DCC's Board to pay additional attention to the assessment and handling of hazard and risk, when the services in question are being provided by any contractor. For example, the Board will have to appoint a Water Quality Committee, to include independent experts on public health and operational aspects of water supply. Its findings should be reported to DCC's Board and attached to its annual report to the DWI and EA. The Board should inform the DWI at once if it does not implement any of that Committee's recommendations. A similar arrangement is proposed for the oversight of sewerage services provided by outside contractors.

DCC will be required to co-operate with its Reporter (an independent consultant, appointed by DCC with the DGWS's approval). The Reporter will review, audit and challenge the work of the Committees and report to the DGWS and the DWI and EA upon the effectiveness of DCC's internal controls. Similar requirements will apply to the contracting-out of the operation of DCC's sewerage services.

In addition, the DGWS proposes a modification prohibiting DCC from:

- making any arrangement to transfer or delegate any of its functions as a statutory undertaker; and
- relying on the involvement of any contractor to establish that it had taken all reasonable steps, or exercised all due diligence, to avoid the commission of an offence if prosecuted for any criminal offence (for example the supply of water unfit for human consumption).

  The defence would only be available to the extent that it would have applied if no contractor had been involved in the activity concerned.

2. *Arrangements for contracting-out (or outsourcing) of operations necessary for the discharge of DCC's obligations as a water and a sewerage undertaker.*

The DGWS considers it important that DCC pursues proper market-testing of whatever services it chooses to outsource. This requirement will be formalised within the procurement condition.

In addition to the requirement to comply with the DGWS's guidance on internal controls this condition will also require DCC to submit a procurement plan to the DGWS. This plan will have to set out:

- an assessment of the competitiveness of the market in which the contract is being let;
- details of the number, mix and type of current and proposed contracts;
- details of the procurement process including how DCC will maintain a "level playing field" for all prospective tenderers, so that no existing contractor derives any advantage from that position; and
- how DCC will retain control of contractors' operations, including the ability to direct action and assume control of operations when necessary and to ensure the maintenance of assets so that serviceability to customers is maintained.

The plan will have to cover at least the following 3 years. It will be reported upon annually by the independent Reporter (see section 1). The DGWS may decide following a report, that he requires an amended plan to be submitted. In any case, the plan will have to be resubmitted (that is, rolled forward over the following 3 years) at least every eighteen months.

3. *Financial ring-fencing and corporate governance of the appointed business*

As in all acquisitions, the DGWS is concerned to ensure that no actions taken by DCC's owners should jeopardise its ability to go on financing the proper discharge of its functions as a water and a sewerage undertaker. To this end the DGWS proposes to amend DCC's licence to:

- prohibit it from raising any finance for the regulated business which include any "cross-default" obligation without the consent of the DGWS;
- prohibit DCC from holding any investments except those required in the ordinary course of its business; and
- require it to maintain an investment-grade corporate credit rating.

A further modification will require DCC to ensure that its dividends are prudent, in the sense that they do not jeopardise its ability to go on financing its functions and reflect the amount of risk borne by shareholders in financing DCC's activities.

To ensure proper corporate governance DCC will obtain from its owner, undertakings:

- that it will refrain from any action which would put DCC in breach of its licence obligations;
- that there will be at all times on Glas' board a majority of independent, non executive directors; and
- DCC's Board will be required to comply with the Principles of Good Governance and Code of Best Practice as for the time being approved for the purpose of the listing rules of the London Stock Exchange.

4. *Access to comparative information*

To ensure that the DGWS will continue to have access to the information he requires to make comparisons between undertakers in order to assess their relative efficiency (including information from contractors), he has proposed that DCC should obtain from its immediate parent and from either WPDL or Glas, as the case may be, an undertaking that they will provide to DCC information:

- necessary to enable it to comply with the conditions of its Appointment; and
- which the DGWS may reasonably require about the activities and financing of either WPDL or Glas as appropriate.

Furthermore, DCC will be required to

- maintain the listing on a recognised stock exchange of a financial instrument (either a bond or a preference share), although it will be permitted to seek the DGWS's approval to the postponement of that listing, depending upon market conditions. The DGWS has indicated to Glas that, as for the other companies who have this licence modification, the listing of the Bonds will satisfy this condition, given that the Issuer functions exclusively as a special purpose finance vehicle for the regulated water and sewage business; and
- publish the information which would be required to comply with the listing rules of the London Stock Exchange, if DCC were itself a listed company.

5. *Additional proposals provisional upon the successful acquisition of DCC by Glas*

Because Glas's plans are predicated on the pursuance of a single purpose, namely the provision of water and sewerage services, the DGWS proposes to modify DCC's Licence to:

- require DCC to obtain a legally enforceable undertaking from Glas prohibiting Glas and its subsidiaries from making any changes to their Memorandum and Articles of Association without the DGWS's consent; and
- prohibit it, or any other subsidiary of Glas from conducting any other activities of a material nature except those required of or connected with a water and a sewerage undertaker.

Finally, a change to DCC's Licence will be required to reflect the fact that DCC will be wholly debt-financed rather than owned by shareholders. This modification will be to amend the interest-cover test used by the DGWS in the context of Interim Determinations of price limits in determining whether a Regulated Company is able to finance its functions. This will require the DGWS to assume that DCC will fund new expenditure solely by raising new debt finance.

Except for the modifications in Section 5, the changes set out above will be made to DCC's licence regardless of whether the Glas proposals proceed. If Glas is successful in acquiring DCC then the changes set out in Section 5 will also be made.

In an open letter to the DGWS dated 7 March 2001, Glas made a public statement explaining how it had met, or intends in the future to meet, the conditions set out in the Position Paper. This letter included a public commitment to customer benefits, a public statement on Glas's commitment to limiting its activities to the single purpose of providing water and sewerage services, a public commitment to appointing the Members of Glas on the basis of best practice and confirmation that the proposed rights for Bondholders would not impede the DGWS's duty under the WIA. In addition, Glas confirmed that its incentive schemes for executive management would be published in due course and that thereafter the remuneration policy would be disclosed in Glas's annual report.

The Policy of the Assembly towards the Ownership of DCC

On 24 May 2000, the Economic Development Committee and the Environment, Planning and Transport Committee (together, the "**Joint Committee**"), issued a joint statement on the then proposed take-over of Hyder by Nomura International Plc. The statement called on the First Minister to reflect a set of principles (the "**Principles**") in his representations to the OFT regarding any proposed acquisition of Hyder.

The Principles state that any new company should:

- preserve the integrity and identity of Hyder as a distinctively Welsh business and keep its headquarters in Wales;
- preserve the maximum number of jobs and, as a minimum, limit the number of job losses to those already announced by Hyder and agreed with trade unions;
- be committed to investment and development of the regulated and non-regulated businesses of Hyder;
- as a minimum maintain Hyder's environmental record and implement the investment programme within existing price limits;
- note that the Assembly has a duty under section 121 of the GWA to promote sustainable development (and that the Assembly has powers to call in applications for planning permission for decision under Section 77 of the UK Town and Country Planning Act 1990 where an application raises planning issues of more than local importance);
- recognise the potential of Welsh water as an economic resource and acknowledge the wish of the Assembly that the people of Wales should benefit from the use of this resource, especially when water is sold outside Wales;
- provide a high quality water and sewerage service for the people of Wales, and a high quality electricity service for the region of Wales that depends on South Wales Electricity plc; and
- operate a fair pricing policy and consider the formula set by the industry regulators as setting the maximum charge to be levied, rather than the norm.

It is these principles, in so far as they relate to the Glas proposals, which formed the basis for the Assembly's subsequent response to Ofwat's consultation paper on Glas (as set out in more detail below).

The Assembly and Glas

Glas produced a memorandum on the Principles which was appended to the open letter sent to the First Minister on 3 November 2000 (following the announcement of the Glas proposals). The memorandum sets out in general terms the manner in which the company's plans will address the Principles.

On 15 November 2000, following the launch of the Ofwat consultation process on 10 November 2000, the Joint Committee held a meeting to discuss the Glas proposals, question Glas and other interested parties about the implications of the proposals and to offer recommendations to the Minister for Environment of the Assembly on issues arising from the proposals. Members were requested to focus on the Principles and the session concluded that the Joint Committee should form a view measured against them.

On 28 November 2000 the Joint Committee issued a statement which said that "*Glas Cymru's proposals measured favourably against the Principles the committees agreed back in May*", and which included an assessment of the Glas Cymru proposals against the Principles. This assessment was also appended to a letter sent by the Joint Committee to the Minister for Environment of the Assembly. The Assembly's response to the Ofwat consultation on the Glas proposals, as set out in a letter from the First Minister to the DGWS dated 22 December 2000 (the "**Assembly Response**"), was also based on this analysis of the Glas proposals and the Principles.

On 11 January 2001 the Glas proposals were discussed in the plenary session of the Assembly and the First Minister summarised the views he had expressed in the Assembly Response:

"*I welcomed the principle of a not-for-profit bond-financed company because it offers potential benefits to customers in the form of lower prices. I welcomed the fact that Glas Cymru's ownership would be Welsh and that its headquarters would be located in Wales, as did both Committees and, by and large, the public Ofwat consultation*".

Following the announcement by Ofwat on 31 January 2001 that it would not block Glas's proposals provided that certain conditions were met, the First Minister and the Minister for the Environment issued a statement in which the First Minister was quoted as saying:

"*I am pleased that this proposal is now being given the go ahead by the water regulator. I particularly welcome the prospect of Dŵr Cymru being owned once again by a company based, managed and controlled from Wales, based on a principle originated in Wales. I also welcome the prospect that this form of not-for-profit, bond-financed company brings of potential benefits in the form of lower prices for customers in Wales...*"

The Assembly has confirmed in a letter to Glas dated 16 March 2001 that it will not exercise its power to block the proposed licence modifications issued by the DGWS on 7 March 2001.

Chapter 12

PROCUREMENT AND OUTSOURCING

THE PROCUREMENT PLAN

Introduction

The ownership of DCC's assets is to be separated from the operation of those assets through the implementation of a procurement plan (the "**Procurement Plan**"). The Procurement Plan is to have two stages: the initial outsourcing plan and a subsequent rolling procurement plan under which the outsourced services are re-tendered. The outsourced services will include the day to day operation and maintenance of its assets and the delivery of customer services, including billing, revenue collection and customer contract management.

OUTSOURCING IN GENERAL

Activities Currently Outsourced

Like most of the water industry, DCC already outsources its capital investment programme and some of its day to day operations, including the operation of its sewerage network and its laboratory and quality sampling activities. DCC's capital investment programme amounts to approximately £240 million every year for the five years to 2005 and over 50 per cent. of it is carried out by six service providers each delivering over £100 million of investment during the five years to 2005. The operation of the sewerage network amounts to between £7 and £8 million every year and is carried out by four service providers for a term of four years until 31 March 2005. The operation of the laboratory and quality sampling activities amounts to £7 million every year and is carried out by one service provider for a term of five years until 2005. In addition, DCC has placed a number of smaller contracts with consultants for investment modelling, leakage and other strategic and technical planning functions. The Procurement Plan will build on this experience. DCC has recently entered into the OSA, the CSA and the ITAs as part of its initial outsourcing policy (see below).

Glas's Procurement Plan Objectives and Strategy

DCC currently outsources work equivalent to over 50 per cent. of its total costs. Glas's Procurement Plan will increase this proportion to around 80 per cent. and will cover both the competitive outsourcing of the initial contracts and the future ongoing outsourcing. Glas intends to publish and maintain the Procurement Plan in line with Ofwat's proposed procurement licence modification (see Chapter 11 under "*Proposed Modifications*"). The overall objective of the Procurement Plan is to obtain best practice and best value from specialist service providers that are the most capable and competitive in the marketplace through competitive outsourcing and ongoing partnership with the service providers. The procurement strategy includes:

- stringent technical and financial pre-qualification of potential service providers;
- an "open book" partnership relationship between DCC and service providers;
- a requirement on service providers to operate the services in accordance with specified quality assurance standards;
- built-in monitoring arrangements to enable DCC's technical operational staff to be fully informed at all times;
- a combination of incentives for out-performance of targets for service delivery and cost efficiency as well as strong sanctions to ensure that service providers do not put service quality at risk;
- no-notice, step-in rights for DCC to assume control of service delivery where DCC reasonably believes that a material risk exists or is likely to exist to health and safety, property or the environment; and
- provisions designed to ensure a smooth hand-over from one service provider to another.

The special responsibilities and duties arising from water legislation reinforce the need for DCC as a Regulated Company to operate at all times with effective internal controls and to comply with and carry out its statutory functions. The Board of DCC will retain full and final responsibility for providing safe and reliable water supply and sewerage services in accordance with its Licence and its statutory obligations.

The most important practical controls on operations which DCC will have are the ability to set best practice requirements for performance, to monitor performance and to "step-in" and take control of operations in the event of any risk of serious shortfall in performance. In addition to these controls, responsibilities as between DCC and service provider will be clear cut and the number of interfaces will be limited. It is intended that DCC will retain the staff and experience necessary to manage contracts and relationships with service providers and to be able to "step-in" and re-let contracts (or bring back "in-house") if necessary.

Glas has agreed with Ofwat certain internal controls to be introduced because essential services are being contracted out (see Chapter 11 under "*Proposed Modifications*"). These controls are supplementary to the general internal controls already required where a Regulated Company provides directly all the essential services. These supplementary controls include the establishment of a Water Quality Committee to advise, review and report on all aspects of DCC's policies for maintaining compliance with Drinking Water Regulations and an Environment Quality Committee, to advise, review and report on DCC's policies for maintaining a safe sewerage system and compliance with the EA's consents. Each committee will include a non-executive member of the board of DCC as its chair, DCC's Operations Director and relevant independent experts.

For the last two years DCC has been operating in the Hyder group within the structure proposed for the initial outsourcing, with service agreements with Hyder Operations and HSL alongside contracts with other service providers. During the last two years DCC has gained the ISO9002 quality management system accreditation and water quality standards have reached best ever levels.

INITIAL OUTSOURCING

DCC put out to tender two contracts: an operations and maintenance contract and a customer services contract. The contracts were tendered as required by the relevant UK and EU procurement rules and notices of a call for competition for these contracts were published in the Official Journal of the European Communities on 23 November 2000 and an amendment to the notice for the operation and maintenance contract was published on 25 November 2000 (the "**OJEC Notices**"). Over 30 expressions of interest were received for each contract. These initial responses were assessed against objective criteria including, in particular, core capabilities and experience. Tender documents were then issued to seven short-listed services providers for each contract, all of which are well established and have proven capabilities. The final bids were submitted on 15 March 2001 and were judged on the basis of the most economically advantageous bid taking into account price, responses to questions on key issues such as risk management, pensions and staff relations, and their transition plan to cover the first three months of the contract. The final decision was made on 28 March 2001 to award the operations and maintenance contract to United Utilities Operational Services Limited (a subsidiary of United Utilities plc) and the customer services contract to Thames Water Services Limited (a subsidiary of Thames Water plc). The respective contracts, the Operation Services Agreement (the "**OSA**") and the Customer Services Agreement (the "**CSA**"), were entered into on 29 March 2001 and will run for four years until 31 March 2005, although there will be an option to split out North Wales operations and maintenance services a year early. The material terms of the OSA and the CSA are summarised below.

Summary of Operation Services Agreement and the Customer Services Agreement

The OSA and the CSA (each a "**Service Agreement**" and together the "**Service Agreements**"), entered into by DCC are summarised below. Defined terms used in this summary shall have the same meanings given to them in the relevant Service Agreement unless otherwise defined in this document except in the case of "Issuer" which means the person who issues a Performance Bond in favour of DCC in relation to the Operator's or the Service Provider's performance of the Service Agreement and "Guarantor" which means the person who enters into a Parent Company Guarantee in favour of DCC in relation to a Contractor's performance of the relevant Service Agreements.

Term

Each Service Agreement commenced on 1 April 2001 and has a scheduled expiry date of 31 March 2005 unless either it is terminated (see below) or DCC exercises its option to extend the term for a further period of up to 12 months.

Scope of Services

The Contractor under the OSA (the "**Operator**") is obliged to perform all tasks necessary for the day to day operation of the Facilities other than the preparation of regulatory submissions, statutory and regulatory reporting, administration of the Licence and other regulatory functions, laboratory services,

operations support bureau and telemetry, which are to be carried out by DCC, although DCC shall be entitled to outsource competitively any of the Services to be provided by the Operator during the term in accordance with the Procurement Plan and the terms of the OSA.

The Contractor under the CSA (the "**Service Provider**") is obliged to carry out the Services, which include maintaining a record of every water service and sewerage service provided by DCC, operating and managing the payment processing system, the credit management process and the Customer Contact Centre, maintaining a team dedicated to revenue protection, maintaining a team to operate, manage and maintain the meter option processes and maintaining and updating all records relating to meter installation and renewals.

DCC's Obligations

In addition to the obligation to make payment to the Contractors, DCC's obligations under the Service Agreements include providing access to the Facilities, providing information, capital maintenance expenditure, managing and submitting regulatory filings, maintaining the Licence in full force and effect, complying with the terms of the Licence and with Legal and Regulatory Requirements, tariff policy and vetting and providing all reasonable liaison and co-operation in connection with the provision of the Services by the Contractors.

Under the OSA, DCC will also implement the Capital Works Programme and any planned capital maintenance and reactive maintenance (unless the Operator is invited by DCC to bid to carry out the Additional Services and is successful in that bid). DCC retains an absolute discretion as to the filing and content of any submissions to the DGWS.

Remuneration

The Contractors shall be entitled to remuneration calculated in accordance with a formula based on the amounts allowed to them for each of the four years indexed in line with inflation and subject to adjustments in line with performance. Their remuneration is based on output and other standards (including KPIs), Legal and Regulatory Requirements and the Owner's Policies. If additional output or standards are adopted, or there is a change in Policy or Relevant Legal and Regulatory Requirements which results in a material (i.e. more than £50,000) increase or decrease in the cost of performing the Services, this will result in an increase or decrease in the relevant Contractor's remuneration as agreed between the parties or failing agreement, dispute resolution. If an Outsourcing Contract is awarded to a third party, the Operator's remuneration will be reduced (if applicable) by the Outsourcing Cost.

Limitations on Liability

Neither party is liable to the other for loss of profit, loss of revenue, loss of goodwill, loss of opportunity or other indirect or consequential loss except in relation to DCC's ability to make Performance Adjustments, liability for death or personal injury resulting from negligence under the Service Agreement and, in the case of the CSA only, DCC's right to claim lost revenue on termination for Service Provider breach.

The total aggregate liability of the parties shall not exceed £50 million under the OSA and £10 million under the CSA. This cap on liability does not apply to DCC's obligation to pay the Contractor for the Services and Equipment on termination, the Operators' obligation to pay DCC for the Transferred Equipment and Owned Vehicles or the Service Providers' obligation to pay DCC for the Equipment and Owned Vehicles, on the Start Date, any liability in respect of physical damage to the Facilities caused by a breach of the relevant Service Agreement, any liability the Contractor may have under the indemnity given in favour of DCC in respect of loss or damage resulting from accidents or injury to personnel, third parties or third party property in the course of performing their respective obligations (unless DCC takes any prejudicial action after the Contractor has taken over conduct of the proceedings), any liability DCC has under the indemnity given in favour of the Contractor to cover any loss or damage caused by DCC exercising its rights to step-in and/or liability for death or personal injury of any person resulting from negligence.

The maximum Performance Adjustment, by which the Contractor's remuneration can be reduced due to their failure to meet the KPIs is capped at £4,000,000 per annum under the OSA and £750,000 per annum under the CSA.

Suspension

The Service Provider may, upon giving at least 7 days' notice of its intention to do so, suspend performance of the Services under the OSA if DCC fails to make payment of any amount by the final date for payment and has not given a notice of intention to withhold the amount due. The only other rights to suspend performance of the Services under the OSA are for reasons of Force Majeure or DCC's right to step-in.

Termination

Each Service Agreement may be terminated by either DCC or the relevant Contractor (as applicable) on the following grounds:

(i) insolvency of DCC, the Contractor or the relevant Guarantor (if, in the case of the Guarantor's insolvency, the Contractor has failed to provide a replacement bond or guarantee as required under the relevant Service Agreement);

(ii) an event of Force Majeure has occurred and continued for at least 180 days (or such shorter period as may be agreed between the parties) and is continuing;

(iii) DCC or the Contractor commits any material or persistent breach of its obligations under the relevant Service Agreement;

(iv) DCC or the Contractor fails to pay any sum, which is not disputed in good faith, due to the relevant party within 80 days after the due date for payment; or

(v) DCC ceases to hold the Licence or ceases to be a water or sewerage undertaker.

In addition, DCC may terminate the relevant Service Agreement on the following grounds:

(vi) the Contractor commits any Gross Negligence or Wilful Default;

(vii) the Contractor abandons provision of the Services;

(viii) the Guarantor/Issuer ceases to maintain an investment grade Credit Rating and the Contractor has failed to provide a replacement bond or guarantee as required under the relevant Service Agreement;

(ix) a Change in Control of the Contractor or the Guarantor occurs to which the DGWS has objected and, in the case of a Change in Control of a Guarantor, the Contractor has failed to provide a replacement guarantee as required pursuant to the relevant Service Agreement;

(x) a Guarantor repudiates in writing the Parent Company Guarantee (and the relevant Contractor has not provided a replacement bond or guarantee as required under the relevant Service Agreement) or fails to pay any sum due under a Parent Company Guarantee; or

(xi) in the case of the CSA, the Service Provider commits any material or persistent breach of the Billing KPIs.

In addition the Contractor may terminate the relevant Service Agreement on the following grounds:

(xii) the Licence is modified or there is a change to DCC's Policies which, in either case, has a material adverse effect on the Contractor's ability to provide the Services; or

(xiii) DCC ceases to be responsible for any significant function to which any material part of the Services relates to the extent that it renders impracticable or impossible the performance of the Services by the Contractor.

There is a 10 day period to remedy under (iv) and (xi) above. There is a 90 day period to remedy under (iii), (viii) and (xii) above (or in the case of (iii) and (xii) such shorter period as may be prescribed or such longer period agreed by the DGWS for remedying the breach).

Step-in

If DCC reasonably believes that it needs to take action in connection with the Services because: (a) in the case of the OSA, a material risk exists or is likely to exist to the health and safety of person or property or to the environment and/or to safeguard the carrying out of its statutory functions; or (b) in the case of the CSA, the failure by the Service Provider to meet the Billing KPIs, DCC may, acting reasonably, take such steps to remedy or mitigate as it considers necessary (either itself or by engaging others).

Subcontracting

The Contractors are not entitled to sub-contract any of their obligations without DCC's consent as to the identity of the sub-contractor and the terms of the sub-contract. DCC can require the Contractor to procure subcontractors (other than counterparties to Owner Agreements and Novated Agreements) to enter into a Direct Agreement with DCC.

On the Start Date, each Contractor is required to execute a deed of novation under which each accepts the transfer to it of all DCC's rights, obligations and liabilities under, in the case of the Operator, the OSA ITA (as defined below), the HSL and Owner Agreements and, in the case of the Service Provider, the CSA ITA (as defined below) and the Novated Agreements.

Assignment and Financing

No Party may assign all or any of their rights under the relevant Service Agreement without the prior written consent of the other relevant Party unless the assignment is to another member of their group. DCC is entitled to create rights of security over a Service Agreement in favour of a potential or existing lender to DCC or any of its Group Companies.

Parent Company Guarantee/Performance Bond

The Operator and the Service Provider are to provide in an amount of £50,000,000 and £10,000,000 respectively either a Parent Company Guarantee or Performance Bond (depending on the successful bidder's preferred option). The Guarantor or the Issuer (as applicable) must possess a Minimum Credit Rating of BBB- (Standard & Poor's), Baa3 (Moody's) or BBB- (Fitch).

Insurance

DCC is required to take out and maintain all insurances required by law or which a reasonable and prudent person holding the Licence would take out and maintain. DCC is required to procure that the Contractor is a co-insured on all such insurances and has the benefit of a waiver of rights of subrogation. The Contractor is required to take out and maintain employer's liability insurance, public liability insurance and motor vehicle insurance.

Force Majeure

A party's obligations which are materially prevented, hindered or delayed by a Force Majeure Event shall be suspended without liability for a period equal to the Force Majeure Event. DCC indemnifies the Contractor for any additional costs arising by reason of a Force Majeure Event to the extent that such costs are recoverable by DCC as permitted by the Regulator. DCC shall only be obliged to pay the remuneration to the extent that the Services are actually performed.

Governing Law and Dispute Resolution

The Service Agreements are governed by English law. Disputes under the OSA are to be resolved in the first instance by negotiation, failing that by adjudication, and finally by arbitration. Disputes under the CSA are to be resolved by negotiation or, failing that, by arbitration.

IT Services Agreements

The IT Services Agreement (the "**DCC ITA**"), the IT Services Agreement in relation to Operation Services to be provided under the OSA (the "**OSA ITA**") and the IT Services Agreement in relation to Customer Services to be provided under the CSA (the "**CSA ITA**" and together with the DCC ITA and the OSA ITA, the "**ITAs**") were entered into on 12 February 2001 by DCC and HSL. HSL's rights and obligations will be novated to Logica. DCC's rights and obligations under the OSA ITA were novated on 29 March 2001 to the Operator under the OSA. DCC's rights and obligations under the CSA ITA were novated on 29 March 2001 to the Service Provider under the CSA. The DCC ITA will remain with DCC. For this purpose, terms defined in this summary shall have the same meanings given to them in the ITAs.

Term

The OSA ITA and the CSA ITA continue in force for so long as the Contractor continues to provide Services under the relevant Service Agreement unless terminated in accordance with their terms or the parties agree to extend them. The DCC ITA continues until 31 March, 2005 unless terminated or extended by agreement.

Scope of Services

The Services include generic activities, application development, application operators, desktop, voice problem resolution and support, printing output and mail management.

DCC's Obligations

In addition to the obligations to make payment to HSL, DCC's obligations include providing HSL with Company Data, information, materials and resources reasonably required by HSL and which is in DCC's custody or control and allowing HSL access to its premises and personnel.

Remuneration

HSL shall be entitled to the Charges set out in Schedule 2 of the relevant ITA, such charges in the second and each subsequent year to be adjusted in accordance with a formula based on the percentage increase in RPI. Should HSL fail to comply within a target limit for Service Levels or KPIs, part of the Charges paid to HSL shall be rebated.

Limitations on Liability

No party shall be liable to the other for loss of profit, loss of goodwill or loss of opportunity or other indirect or consequential losses except in relation to DCC's right to deduct rebates, HSL's right to indirect or consequential losses on termination for DCC breach, HSL's right to claim for any loss or damage should DCC exercise its rights to step-in, liability for death or personal injury resulting from negligence, and under the CSA ITA only, DCC's right to claim loss of revenue.

The total aggregate liability of the parties is capped at £5 million under the OSA ITA and CSA ITA and £2 million under the DCC ITA. This cap does not apply to DCC's liability to pay the charges, HSL's liability in respect of physical damage to the Facilities caused by a breach of the relevant ITA Agreement by HSL, any liability resulting from a third party claim, DCC's liability to indemnify HSL should it cause loss or damage having exercised its right to step-in and any liability for death or personal injury resulting from negligence.

Termination by DCC

DCC may terminate the ITAs on the grounds that HSL is insolvent, HSL commits any act of Gross Negligence or Wilful Default, a Force Majeure Event has occurred and continued for at least 180 days (or such shorter period as may be agreed by the parties) and is continuing, HSL abandons provision of the Services, HSL commits any material or persistent breach of its obligations under the relevant ITA Agreement, HSL fails to make payment of any sum due to DCC within 60 days of it having become due or HSL commits any of the Defaults in Schedule 11 of the relevant ITA.

DCC may also terminate the OSA ITA and the CSA ITA on termination of the OSA or the CSA respectively.

Termination by HSL

HSL may terminate the ITAs on the grounds that DCC is insolvent, DCC's failure to pay any sum due under the relevant ITA Agreement within 60 days after such sum having become due, a Force Majeure Event has occurred and continued for at least 180 days (or such shorter period as may be agreed between the parties) and is continuing or DCC commits any material or persistent breach of its obligations under the relevant ITA Agreement. HSL may also terminate the OSA ITA or the CSA ITA on termination of the OSA or the CSA, as applicable.

Step-in

If DCC reasonably believes that it needs to take action in connection with the Services to safeguard the carrying out of its statutory functions and/or the Services under the OSA ITA or the CSA ITA or to remedy a Default, DCC may take such action as it considers necessary either itself or by engaging others.

Assignment and Financing

The prior written consent of the other party (such consent not to be unreasonably withheld or delayed) is required before a party can assign its rights under the relevant ITA Agreement except in respect of assignment to an affiliate, security in favour of a lender and DCC's right to novate the OSA ITA to the Operator or the CSA ITA to the Service Provider.

Insurance

HSL is required to take out and maintain all insurances required by law or which would be effected by a reasonable and prudent person providing the Services.

Force Majeure

A party's obligations which are materially prevented, hindered or delayed by an event of Force Majeure shall be suspended without liability for a period equal to the duration of the Force Majeure event.

Governing Law/Dispute Resolution

Each ITA Agreement is governed by English law. If the parties do not resolve disputes by negotiation, they are resolved by arbitration. Provision is made for disputes occurring under the OSA ITA or CSA ITA to be joined to any disputes under the OSA or the CSA as applicable.

Contract for Differences

DCC, WPD Finance and Glas Securities have entered into the CfD as of 14 March 2001 (which was amended and restated on 3 April 2001) in order to fix approximately 58 per cent. of DCC's operation and maintenance costs for providing water and sewerage services under its Licence (which comprises of the cost of water operations, customer services and information technology costs) from 1 April 2001 until the next price review by Ofwat in 2005, final payment to be settled around 30 June 2005 (as referred to below). For the avoidance of doubt, these operation and maintenance costs do not include capital maintenance costs or any other capital expenditure costs.

The CfD supplements the terms of the 1992 ISDA Master Agreement (the "**ISDA Agreement**") (which is not discussed in this summary) and Schedule. The principal terms of the CfD are set out below. Unless the context requires otherwise, terms used but not defined in this summary have the meanings given in the ISDA Agreement.

Payments under the CfD

Payments under the CfD are made for each year ending on 31 March on the following 30 June (as modified in accordance with the Following Business Day Convention (as defined in the 2000 ISDA Definitions)).

Amount payable by DCC

The annual amount payable by DCC will be as follows:

2001/02	£118.44 million
2002/03	£114.35 million
2003/04	£110.25 million
2004/05	£105.63 million,

as adjusted for inflation in the same way as in the Service Agreements.

Amount payable by WPD Finance

The annual amount payable by WPD Finance will be the aggregate of the Pre-Award Payments, and the Post Award Payments.

Pre-Award Payments

This is the aggregate amount of operating costs incurred by DCC in the relevant year falling in the period prior to the award of the Service Agreements for providing water and sewerage services and customer services to the area specified in its Licence as a Regulated Company which is agreed to be £9,870,000 per month (in September 2000 prices) as adjusted for inflation in the same way as in the Service Agreements.

The above figure, when annualised, equals the amount payable by DCC in respect of the same period. As a result, in the period before the award of the Service Agreements, there will be no net payment under the CfD.

Post Award Payments

This is the aggregate amount paid in the relevant year by DCC to the Contractors under the Service Agreements or, in the event of termination of the Service Agreements, the amount which would have been paid to such Contractors during the relevant year, assuming that there is no outsourcing, but subject to adjustment for inflation and excluding:

- any payments under the DCC ITA;
- the amount of any adjustment to payments under the Service Agreements to reflect the performance of the relevant Contractor;
- any costs taken into account in determining the amount of the Pre-Award Payments;
- any costs arising from any variation to the Service Agreements;
- any costs arising from any claim for damages;
- any costs arising from the termination of the Service Agreements; and
- the cost of any capital maintenance or other capital expenditure incurred by DCC not required to be provided by the Operator under the form of the OSA put out to tender.

Within 30 days of the execution of both Service Agreements, DCC and WPD Finance will use their reasonable endeavours to agree the annual amount payable by WPD Finance (at September 2000 prices) under the CfD. If such amount is agreed, the agreed amount, subject only to adjustment for inflation in the same way as in the Service Agreements, will replace the provisions summarised above in this paragraph entitled "*Post Award Payments*".

On the basis of the OSA and CSA entered into on 29 March 2001, it is expected, on a net basis, that annual amounts will be payable by DCC to WPD Finance of £7.8 million, £8.1 million, £8.8 million and £10.5 million (each in September 2000 prices) over the term of the CfD.

Credit Support

WPD Finance's payment obligations under the CfD are unconditionally and irrevocably guaranteed by WPDH under a Guarantee dated as of 14 March 2001. There is no Credit Support Provider in relation to DCC.

Indemnity to Glas Securities in respect of Non-procurement of IT Services

WPD Finance shall indemnify Glas Securities for itself and on trust for Glas and its subsidiaries (each a "**Glas Company**") for any loss, damage, cost (save to the extent recovered under the CfD), claim, expense, liability, penalty or fines (together the "**Indemnified Loss**") incurred or borne by any Glas Company as a direct result of any of the ITAs not having been awarded in accordance with applicable EC and UK public procurement legislation, including any sums which DCC is required to pay, whether by way of indemnity or otherwise, to the parties to the Service Agreements, any legal costs and the reasonable costs and expenses of such other advisors to any Glas Company as may be agreed by WPD Finance (whose agreement is not to be unreasonably withheld), which arise as a direct result of the ITAs not having been awarded in accordance with such legislation.

WPD Finance may, at its option and at its own expense, have conduct of all negotiations for the settlement of any claims brought against any Glas Company in respect of the above matters and any related litigation. If there is a cost difference under any replacement DCC ITA awarded following an action under the legislation referred to above in relation to the DCC ITA awarded to HSL, any increased costs shall be borne by WPD Finance. Any reduced costs, however, shall be paid by DCC to WPD Finance. WPD Finance's liability under the indemnity shall not extend to any liability for any loss of profit, loss of use, loss of production, loss of contracts (other than the ITAs or the Service Agreements), increased costs of funding or for any consequential loss.

Glas Securities is party to the CfD only for the purposes of the provisions summarised above and, for the purposes of enforcing its rights under those provisions, and a number of specified provisions of the ISDA Agreement. Breach of the indemnity provisions, summarised above cannot cause an Event of Default or Termination Event. These provisions survive early termination or scheduled expiry of the CfD.

Voluntary Termination

The usual close-out mechanism in the ISDA Agreement will not apply on a voluntary termination. Accordingly, if either WPD Finance or DCC wish to terminate the CfD before its scheduled expiry, it will have to agree with the other what, if any, payment will be made.

FUTURE OUTSOURCING

Glas intends that all the objectives, strategies, controls and management mechanisms outlined above in ''*Outsourcing in General*'' if proven successful will continue in respect of the future outsourcing.

The first phase of retendering for operation and maintenance in North Wales is intended by Glas to take place during 2002–2003 and tender bids will be obtained by around May 2003. Glas plans that retendering for the remaining future outsourced contracts will take place during 2003-2004 but in any event, that tender bids for the next generation of contracts will be obtained by around March 2004 to enable the new market tested contract prices to be available for DCC's business plan and before Ofwat sets the next price determination. Before this stage, Glas will consider the performance of the current outsourced contracts in order to decide whether the same format will be repeated or whether the operations and maintenance contract should be split into a number of smaller regional contracts and, if so, how many regional contracts.

For the decision to be taken to split the operations and maintenance contract into more than one regional contract certain criteria will have to be met in order to achieve the correct balance of scale and competition as well as giving the back-up required to have effective ''step-in'' resources from one operator to another. If smaller regional contracts are opted for it is anticipated that there will be no more than six operations and maintenance contracts: for example, two or three ''source to tap'' water supply contracts and two or three wastewater treatment contracts. However, within any such region there will only be one ''source to tap'' contract. There would also be for the whole of the appointed area one customer services contract, one laboratory and sampling contract and one ''data maintenance'' contract.

The geographical scope for each of the water and the wastewater contracts would be the same. This, as well as the possible mix of contracts, would mean that any possible economies of scale could be accounted for in the bidding process. The mix of contracts also would mean that it would be possible to compare performance between operations and maintenance service providers and to replace a failing service provider at short notice. Finally, Glas intends that capital maintenance expenditure (which will be most of DCC's future capital investment programme) will be outsourced.

Glas does not anticipate that DCC will be able to enter into any arrangements such as the CfD to fix operation and maintenance costs of DCC upon expiry of the CfD. This may affect DCC's future revenues.

THE UTILITIES REGULATIONS

The Utilities Contracts Regulations 1996 (SI 1946/2911) which implement Council Directives 93/38/EEC and 92/13/EEC (the ''**Utilities Regulations**'') apply whenever a utility, such as DCC, seeks offers in relation to a proposed supply, works or ''Part A'' services contract (other than a contract excluded from the operation of the Regulations). Where the Utilities Regulations apply, a utility seeking offers shall make a call for competition which involves the publication of a notice in the OJEC. As required by the Utilities Regulations, DCC published the OJEC Notices in relation to both the Service Agreements with the intention of selecting the successful Contractor under each Service Agreement by the end of March 2001.

In relation to services contracts, the call for competition requirement only applies where the services in question fall within ''Part A'' categories, as specified in Schedule 4 of the Utilities Regulations. A significant exclusion to the application of the Utilities Regulations is the exclusion for services contracts awarded to affiliated undertakings. For the exclusion to apply, it is necessary to show that the affiliate in question is a ''relevant affiliated undertaking''. In cases where the utility is subject to the Seventh Council Directive 83/8349/EEC on Consolidated Accounts, the affiliated undertaking is any undertaking whose accounts are consolidated with those of the utility. In other cases, an affiliated undertaking means a parent undertaking, a subsidiary undertaking or a ''fellow subsidiary'' undertaking of the utility (i.e. where both are subsidiary undertakings of the same parent undertaking). A relevant affiliated undertaking is one which provides services principally to one or more

of its affiliated undertakings. In the case of an undertaking which has been in existence for 36 months or more, it is taken to be providing services ''principally'' if, for the preceding 36 months, 80 per cent. or more of its relevant services were provided to group companies.

In the judgment of Mr Justice Langley in *Severn Trent plc -v- Dŵr Cymru, WPD Holdings UK and United Utilities plc* of 10 October 2000, the Utilities Regulation were held to apply to a procurement strategy which was proposed to be implemented by DCC, following the public takeover of its parent company, Hyder, by WPDL. While the Judge did not try the issue of whether the relevant services were Part A services (and therefore did not conclude definitively that the Utilities Regulations applied to the arrangements), the Judge found that Severn Trent was able to pursue its application to prevent DCC from concluding an operation and maintenance agreement with a new company called UUco on the basis of the Utilities Regulations.

The arrangements which were the subject of the litigation comprised, firstly, DCC's entering into a seven year operation and maintenance agreement with a new fellow group subsidiary, UUco, followed by, secondly, the sale of that subsidiary to United Utilities. The operation and maintenance agreement in question was to be subject to a progressive procurement plan regulated by a procurement condition agreed with Ofwat.

The Judge found that the operation and maintenance agreement could not, on the facts, be considered merely incidental to the sale of UUco and did not thereby fall outside the scope of the Utilities Regulations. The Judge also found that the arrangement fell outside both the spirit and wording of the relevant affiliates exemption, since at no time could it be sensibly said that UUco had as one of its activities the provision of services principally to DCC as affiliate. The Judge concluded that the raison d'être of UUco was to provide a vehicle for the services in question to be provided by a non-affiliate. Following the judgement in the Severn Trent case, DCC announced, on 20 October 2000, that it would go out to competitive tender on the Service Agreements.

In light of the *Severn Trent* judgement, there is a degree of uncertainty surrounding the application of the Utilities Regulations to the ITAs as these have not been the subject of a call for competition. Whilst DCC believes, and has been advised, that there are arguments that the Utilities Regulations would not apply, there can be no guarantee that a court would necessarily share this view. The remedy set out in the Utilities Regulations for breach thereof, where the relevant contract has been entered into, is damages payable to a provider who has suffered loss or damage as a consequence of the breach. DCC considers that the amount of any potential damages claim would not be material in the context of the issue of the Bonds because the profit margin that is projected could be earned under the ITAs is less than £1.5million per annum. There is an additional risk that, in the event of a claim brought against DCC, the court would set aside the ITAs. In these circumstances, DCC would be required to tender for information technology support services in accordance with the Utilities Regulations. DCC believes, and has been advised, that if the ITAs were set aside by an order of a court, such an order would not invalidate the tender process of the Service Agreements or the contracts entered into thereto. Nevertheless, as described in more detail above, under the CfD, WPD Finance will indemnify Glas Securities on behalf of each Glas Company against any loss, damage, cost (save to the extent that it is otherwise covered under the swap transaction), claim, expense, liability, penalty or fines incurred by or borne by any Glas Company as a direct result of any one, or any combination, of the ITAs not having been awarded in accordance with the relevant procurement law.

CHAPTER 13

TAX CONSIDERATIONS

The following is a summary of the UK withholding taxation treatment at the date of this Information Memorandum in relation to payments of principal and interest in respect of the Bonds and Cayman Islands taxation treatment of the Issuer. These comments do not deal with other UK 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 Sub-Class of Bonds as specified in the relevant Pricing Supplement may affect the tax treatment of that and other Sub-Classes or Classes of Bonds. This summary as it applies to UK taxation is based upon UK law and Inland Revenue practice as in effect on the date of this Information Memorandum and, together with Cayman Islands taxation treatment of the Issuer, 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 UK 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 UK 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 UK.

Prospective purchasers who are in any doubt as to their tax position should consult their professional advisers.

United Kingdom

Payment Of Interest By The Issuer

As a result of provisions contained in the UK Finance Act 2000, the only requirement that has to be satisfied in order for interest payable on the Bonds to be paid free of UK withholding tax is that the Bonds are listed on a recognised stock exchange within the meaning of section 841 of the UK Income and Corporation Taxes Act 1988. The Luxembourg Stock Exchange is such a recognised stock exchange. If this requirement is not satisfied as at the date interest on the Bonds is paid, then such interest may be paid under deduction of UK income tax at the lower rate (currently 20 per cent.) subject to such relief as may be available under the provisions of any applicable double taxation treaty. If UK withholding tax is imposed, then the Issuer will not pay any additional amounts under the terms of the Bonds.

As a result of provisions contained in the UK Finance Bill 2001 printed on 13 March 2001, and if such provisions are enacted in their present form, the Issuer will be able to pay interest on the Bonds to Bondholders whom it reasonably believes are within the charge to UK corporation tax free of UK withholding tax, whether or not the Bonds are listed on a recognised stock exchange.

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 UK withholding tax.

Where Bonds are issued with a redemption premium, as opposed to being issued at discount, then any such element of premium may constitute a payment of interest. Payments of interest are subject to UK withholding tax as outlined above (and also subject to the exemption outlined above).

Provision Of Information By UK Paying And Collecting Agents

Where interest is paid on the Bonds by or through a UK paying or collecting agent, such agent may be required to furnish to the Inland Revenue details of the amounts of interest which they have paid or collected and the names and addresses of the persons to whom such interest has been paid or on whose behalf such interest has been collected, together with such further information as may be prescribed by regulations to be made by the Inland Revenue (which may include details of the names and addresses of the persons who are beneficially entitled to any such interest paid or collected by the paying or collecting agents). In certain circumstances, the Inland Revenue might exchange such information with the tax authorities of other jurisdictions.

Payments By Financial Guarantors Under The Bond Policies

If a Financial Guarantor makes any payments in respect of scheduled payments of principal and interest on the Class A Bonds (or other amounts due under the Class A Bonds other than the repayment of amounts subscribed for the Class A Bonds), such payments may be subject to UK withholding tax subject to such relief as may be available under the provisions of any applicable double taxation treaty. Such payments by the Financial Guarantors may not be eligible for the exemption from UK withholding tax described above. If UK withholding tax is imposed, then the Financial Guarantor will not pay any additional amounts under the Bond Policies.

Proposed EU Directive On The Taxation Of Savings Income

The European Union is currently considering proposals for a new directive regarding the taxation of savings income. Subject to a number of important conditions being met, it is proposed that Member States will be required to provide to the tax authorities of another Member State details of payments of interest or other similar income paid by a person within its jurisdiction to an individual resident in that other Member State, subject to the right of certain Member States to opt instead for a withholding system for a transitional period in relation to such payments. The proposals are not yet final, and they may be subject to further amendment and/or clarification.

Cayman Islands

The Issuer has been incorporated under the laws of the Cayman Islands as an exempted company and, as such, the Issuer has obtained an undertaking from the Governor in Council of the Cayman Islands substantially in the following form:

"The Tax Concessions Law
(1999 Revision)
Undertaking as to Tax Concessions

In accordance with Section 6 of the Tax Concessions Law (1999 Revision), the Governor in Council undertakes with Dwr Cymru (Financing) Limited (the "Company"):

(a) that no Law which is hereafter enacted in the Islands imposing any tax to be levied on profits, income gains or appreciations shall apply to the Company or its operations; and

(b) in addition, that no tax to be levied on profits, income gains or appreciations or which is in the nature of estate duty or inheritance tax shall be payable:

    (i) on or in respect of the shares debentures or other obligations of the Company; or

    (ii) by way of the withholding in whole or in part of any relevant payment as defined in Section 6(3) the Tax Concessions Law (1999 Revision).

The concessions shall be for a period of twenty years from 27 February, 2001.

Governor in Council"

CHAPTER 14

SUBSCRIPTION AND SALE

Subscription and Sale

Bonds (other than the Class R Bonds) may be sold from time to time by the Issuer to any one or more of The Royal Bank of Scotland plc or Salomon Brothers International Limited and any other dealer appointed from time to time (collectively, the "**Dealers**") pursuant to the dealership agreement dated on or about the date of this Information Memorandum made between, *inter alia*, DCC, the Issuer and the Co-Arrangers (the "**Dealership Agreement**"). The arrangements under which a particular Sub-Class of Bonds may from time to time be agreed to be sold by the Issuer to, and purchased by, particular Dealers are set out in the Dealership Agreement and the subscription agreements relating to each Sub-Class of Bonds. The Pricing Supplements will, *inter alia*, make provision for the form and Conditions of the relevant Bonds and the price at which such Bonds will be purchased by the applicable Dealers. The Dealership Agreement makes provision for the resignation or termination of appointment of existing Dealers and for the appointment of additional or other Dealers either generally in respect of the Programme or in relation to a particular Sub-Class, Class or Series of Bonds.

Pursuant to a subscription agreement in respect of the Series 1 Sub-Class A-1 Bonds dated on or about the date of this Information Memorandum and made between the Issuer, the Co-Arrangers and Barclays Bank PLC ("**Barclays**"), Barclays will be appointed a Dealer in addition to the Co-Arrangers with respect to the Series 1 Sub-Class A1 Bonds. Pursuant to a subscription agreement in respect of the Series 1 Sub-Class A-2 Bonds dated on or about the date of this Information Memorandum and made between the Issuer, the Co-Arrangers, Lehman Brothers International (Europe) ("**Lehman Brothers**") and Banc of America Securities Limited ("**BoA**"), Lehman Brothers and BoA will be appointed Dealers in addition to the Co-Arrangers in respect of the Series 1 Sub-Class A2 Bonds.

Class R Bonds

Citibank, N.A. (together with any other underwriters appointed from time to time by the Issuer, the "**Class R Underwriters**") pursuant to an underwriting agreement dated on or about the date of this Information Memorandum between, *inter alios*, the Class R Underwriters, DCC and the Issuer (the "**Class R Underwriting Agreement**") may, for a period from and including the Initial Issue Date to and including 31 March 2006, subject to certain conditions, agree to subscribe or purchase, from time to time, and pay for the Class R Bonds offered for sale or resale by the Issuer from time to time, up to an underwriting commitment of £100,000,000.

The Class R Underwriters from time to time may novate all or part of their underwriting commitments to persons who meet certain criteria. Such novations shall be effected by the relevant Class R Underwriter and the person to whom such Class R Underwriter proposes to novate its underwriting commitment completing a novation certificate and delivering the same to the Issuer and each other Class R Underwriter, who will then execute the same. Such novation shall take effect on the later of the date upon which the last person executes the novation certificate or the date specified in such novation certificate.

On the Initial Issue Date, the Class R Underwriters will subscribe and pay for all of the Class R Bonds. Such Class R Bonds will be immediately repurchased, but not cancelled, by the Issuer on the Initial Issue Date.

Subject as described below (unless otherwise agreed), the conditions precedent to the resale of any Class R Bonds to the Class R Underwriters will include:

- no Issuer Event of Default under the Bonds has occurred and is subsisting immediately prior to the sale of the Class R Bonds;
- all conditions precedent (other than the sale of the Class R Bonds themselves) to the making of the relevant R Advances under the Intercompany Loan Agreements have been satisfied; and
- certain other conditions.

It should be noted that if Class R Bonds are subsequently being resold by the Issuer for the sole purpose of financing the Issuer's repurchase of Class R Bonds which have previously been issued or sold, the only condition precedent to the Class R Underwriter purchasing such Class R Bonds will be that no Issuer Event of Default under the Bonds exists.

The Issuer may, upon 30 days' prior written notice to all other parties to the Class R Underwriting Agreement and the payment of any accrued fees, costs and expenses, terminate any amount of the facility provided by the Class R Underwriters thereunder to purchase the Class R Bonds, to the extent that such facility has not been utilised to the extent of Class R Bonds which are outstanding.

The Class R Underwriting Agreement is subject to a number of additional conditions and may be terminated and/or the underwriting facility suspended by the Class R Underwriters in certain circumstances by the Class R Underwriters prior to the Issuer's repurchase at any time of the Class R Bonds. The Issuer (failing whom DCC) has agreed to indemnify the Class R Underwriters against certain liabilities in connection with the offer, sale or repurchase of the Class R Bonds.

United States of America

The Bonds 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, and may include Bonds in bearer form, which 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, or for the account or benefit of, U.S. persons, except in certain transactions permitted by U.S. tax regulations. Terms used in this paragraph have the meanings given to them by Regulation S under the Securities Act, as amended, or the U.S. Internal Revenue Code of 1986 and regulations thereunder as appropriate. Each of the Dealers and each Class R Underwriter has agreed that it will not offer, sell or deliver any Bonds (i) as part of their distribution at any time or (ii) otherwise until 40 days after the completion of the distribution of each Sub-Class, within the United States or to, or for the account or benefit of, U.S. persons except as permitted by the Dealership Agreement or the Class R Underwriting Agreement, as appropriate, and that it will have sent to each dealer to which it sells Bonds during this 40 day period a confirmation or other notice setting forth the restrictions on offers and sales of the Bonds within the United States or to, or the account or benefit of, U.S. persons. In addition, until 40 days after the commencement of the offering, an offer or sale of the Bonds within the United States by any dealer (whether or not participating in the offering) may violate the registration requirements of the Securities Act.

Cayman Islands

No invitation or solicitation will be made to the public in the Cayman Islands to subscribe for the Bonds.

United Kingdom

Each Dealer and Class R Underwriter has represented and agreed that:

(1) ***No offer to public***: it has not offered or sold and will not offer or sell any Bonds to persons in the United Kingdom prior to the expiry of the period of six months from the date of issue of the Bonds, except 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 otherwise in circumstances which have not resulted and will not result in an offer to the public in the United Kingdom within the meaning of the Financial Services Act and the POS Regulations;

(2) ***General compliance***: it has complied and will comply with all applicable provisions of the UK Financial Services Act 1986 with respect to anything done by it in relation to such Bonds in, from or otherwise involving the United Kingdom; and

(3) ***Investment advertisements***: it has only issued or passed on and will only issue or pass on in the United Kingdom any document received by it in connection with the issue of such Bonds, to a person who is of a kind described in article 11(3) of the Financial Services Act 1986 (Investment Advertisements) (Exemptions) Order 1996 (as amended) or is a person to whom such document may otherwise lawfully be issued or passed on.

General

Other than with respect to the listing of the Bonds on the Luxembourg Stock Exchange, no action has been or will be taken in any country or jurisdiction by the Issuer or any of the Other Parties that would permit a public offering of Bonds, or possession or distribution of any offering material in relation thereto, in any country or jurisdiction where action for that purpose is required. Persons into whose hands the Information Memorandum or any Pricing Supplement comes are required by the Issuer and

the Other Parties to comply with all applicable laws and regulations in each country or jurisdiction in or from which they purchase, offer, sell or deliver Bonds or have in their possession or distribute such offering material, in all cases at their own expense.

The Dealership Agreement and the Class R Underwriting Agreement respectively provide that the Dealers and the Class R Underwriters shall not be bound by any of the restrictions relating to any specific jurisdiction (set out above) to the extent that such restrictions shall, as a result of change(s) or change(s) in official interpretation, after the date hereof, in applicable laws and regulations, no longer be applicable but without prejudice to the obligations of the Dealers or the Class R Underwriters above.

Selling restrictions may be supplemented or modified with the agreement of the Issuer. Any such supplement or modification will be set out in the relevant Pricing Supplement (in the case of a supplement or modification relevant only to a particular Sub-Class or Class of Bonds) or (in any other case) in a supplement to this document.

CHAPTER 15

GENERAL INFORMATION

1. Application has been made to list Bonds issued under the Programme on the Luxembourg Stock Exchange and, in connection therewith, the Luxembourg Stock Exchange has assigned registration number 12556 to the Programme. Prior to the listing of any Bonds, the constitutional documents of the Issuer and the legal notice relating to the issue will be registered with the Registrar of the District Court in Luxembourg (*Greffier en Chef du Tribunal d'Arrondissement de et à Luxembourg),* where copies of these documents may be obtained upon request.

2. The establishment of the Programme was authorised by a resolution of the board of directors of the Issuer passed on 3 May 2001. 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.

3. The Bonds have been accepted for clearance through Euroclear and Clearstream, Luxembourg. The appropriate common code and ISIN for each Sub-Class of Bonds allocated by Euroclear and Clearstream, Luxembourg will be specified in the applicable Pricing Supplement. If the Bonds are to clear through an additional or alternative clearing system the appropriate information will be specified in the applicable Pricing Supplement.

4. Bonds and Coupons appertaining thereto will bear a legend substantially to the following effect: ''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 in such legend provide that a United States person who holds a Bond or Coupon generally will not be allowed to deduct any loss realised on the sale, exchange or redemption of such Bond or Coupon and any gain (which might otherwise be characterised as capital gain) recognised on such sale, exchange or redemption will be treated as ordinary income.

5. Neither the Issuer nor DCC is or has been involved in any litigation or arbitration proceedings which have, may have or have had within the period of twelve months preceding the date of this Information Memorandum, a significant effect on the financial position of the Issuer or, as the case may be, DCC nor is the Issuer or DCC aware of any such proceedings as being pending or threatened.

6. The first financial statements of the Issuer will be prepared as of 31 March 2002. The Issuer has not published and does not intend to publish any interim financial statements. It is anticipated that the first published audited annual financial statements and all future audited annual financial statements of the Issuer will be available free of charge in accordance with paragraph 19 below.

7. Since 15 February 2001, the date of its incorporation, there has been no significant change in the financial or trading position, nor any material adverse change in the financial position or prospects, of the Issuer.

8. PricewaterhouseCoopers, as auditors of the Issuer, have given and have not withdrawn their written consent to the inclusion in the Information Memorandum of their auditors' report on the Issuer in the form and context in which it is included herein.

9. The financial statements of DCC have been audited for each of the two financial years immediately preceding the date of this Information Memorandum by PricewaterhouseCoopers and were not qualified. The last published audited annual financial statements and all future financial statements of DCC will be available free of charge in accordance with paragraph 19 below.

10. Other than as disclosed in this Information Memorandum, since 31 March 2000, the date of the last published audited accounts there has been no significant change in the financial or trading position, nor any material adverse change in the financial position or prospects, of DCC.

11. Neither MBIA nor MBIA Insurance Corporation is or has been involved in any litigation or arbitration proceedings which have, may have or have had within the period of twelve months preceding the date of this Information Memorandum, a significant effect on the financial position of MBIA or MBIA Insurance Corporation, nor is MBIA or MBIA Insurance Corporation aware of any such proceedings as being pending or threatened.

12. There has been no significant change in the financial or trading position, nor any material adverse change in the financial position or prospects, of MBIA (which has no subsidiaries) or MBIA Insurance Corporation since 31 December 2000, the date of their most recently audited financial statements.

13. The financial statements of MBIA and MBIA Insurance Corporation have been audited for each of the three financial years immediately preceding the date of this Information Memorandum by PricewaterhouseCoopers and were not qualified.

14. PricewaterhouseCoopers, as auditors of MBIA and MBIA Insurance Corporation, have given and have not withdrawn their written consent to the inclusion in the Information Memorandum of their letters in the form and context in which they are included herein.

15. The issue of the Bond Policies by MBIA in respect of the Class A Bonds to be issued on the Initial Issue Date has been duly authorised by resolution of the meeting of the board of directors of MBIA passed on 13 April 2001.

16. BBV have given and have not withdrawn their written consent to the inclusion in this Information Memorandum of their letter in the form and context in which it is included herein.

17. The Bonds will constitute ''longer term debt securities'' issued in accordance with regulations made under Section 4 of the UK Banking Act 1987. The Issuer is not an ''authorised institution'' or a ''European authorised institution'' as such terms are defined in the UK Banking Act 1987 (Exempt Transactions) Regulations 1997. The Issuer confirms for the purpose of such Regulations, that it:

    (a) has complied with its obligations under the ''relevant rules'' (as defined in such Regulations) in relation to the admission to and continuous listing of the Programme;

    (b) will have complied with its obligations under the relevant rules in relation to the admission to listing of Bonds by the time when such Bonds are so admitted; and

    (c) has not, since the last publication, if any, in compliance with the relevant rules of information about the Programme, any previous issues made under it and listed on the Luxembourg Stock Exchange, or the Bonds, having made reasonable enquiries, become aware of any change in circumstances which could reasonably be regarded as significantly and adversely affecting its ability to meet its obligations as issuer in respect of the Bonds as they fall due.

18. MBIA is not an ''authorised institution'' or a ''European authorised institution'' as such terms are defined in the UK Banking Act 1987 (Exempt Transactions) Regulations 1997.

19. For so long as the Programme remains in effect or any Bonds shall be outstanding, copies of the following documents may be inspected during normal business hours (in the case of Bearer Bonds) at the specified offices of the Principal Paying Agent and the Luxembourg Listing Agent, (in the case of Registered Bonds) at the specified office of the Registrar and the Transfer Agents and (in all cases) at the registered office of the Issuer or the Bond Trustee, and, in the case of the documents referred to in items (e) to (j) inclusive, for collection free of charge during normal business hours at the specified office of the Luxembourg Listing Agent and the office of the Issuer, namely:

    (a) the Issuer's Memorandum and Articles of Association;

    (b) DCC's Memorandum and Articles of Association;

    (c) English translation of MBIA's Articles of Association and By-laws;

    (d) MBIA Insurance Corporation's By-laws;

    (e) the auditors' report from PricewaterhouseCoopers in respect of the Issuer included in Appendix G, the latest annual audited financial statements of DCC and the Issuer and, in the case of DCC, its latest unaudited semi-annual financial statements;

    (f) the latest annual audited financial statements of MBIA and MBIA Insurance Corporation and, in the case of MBIA Insurance Corporation, its latest unaudited quarterly financial statements (MBIA does not publish interim financial statements);

    (g) the accountants' report from PricewaterhouseCoopers included in Appendix C in respect of MBIA's financial statements;

(h) the accountants' report from PricewaterhouseCoopers included in Appendix C in respect of MBIA Insurance Corporation's financial statements;

(i) each Pricing Supplement relating to each Sub-Class of Bonds issued under the Programme;

(j) each Bond Policy and all related Endorsements relating to each Sub-Class of Class A Bonds issued under the Programme;

(k) the Ernst & Young opinion on the DCC Financial Projections;

(l) each Intercompany Loan Agreement relating to each Series of Bonds issued under the Programme;

(m) the Common Terms Agreement;

(n) the DCC STID;

(o) the DCC Deed of Charge;

(p) the Holdings Deed of Charge;

(q) the HUH Deed of Charge (until completion under the Share Purchase Agreement);

(r) the Glas Securities Deed of Charge;

(s) the Glas Deed of Charge;

(t) each Finance Lease;

(u) the Gen Re Swap;

(v) the DCC Account Bank Agreement;

(w) the Trust Deed;

(x) the Master Framework Agreement;

(y) the Issuer Deed of Charge;

(z) the Issuer STID;

(aa) each Liquidity Facility Agreement;

(bb) each Hedging Agreement;

(cc) the Issuer Account Bank Agreement;

(dd) each Subscription Agreement;

(ee) the Class R Underwriting Agreement;

(ff) the Dealership Agreement;

(gg) the Paying Agency Agreement;

(hh) the Tax Deed of Covenant;

(ii) the Issuer Corporate Services Agreement; and

(jj) the Authorised Loan Facilities.

20. Ernst & Young have given and have not withdrawn their written consent to the inclusion in the Information Memorandum of their opinion on the DCC Financial Projections in the form and context in which it is included herein.

Appendix A

Key Characteristics of the Bonds

The ratings attributed below are anticipated ratings only, and may be subject to adjustment by the Rating Agencies when final ratings are published on the Initial Issue Date.

Sub-Class of Bonds

	A1	A2	A3	A4	A5	B1	B2	B3	B4	C1	C2	D1	R
Nominal amount per Bond	£1,000 £10,000 £100,000	£1,000 £10,000 £100,000	$1,000 $10,000 $100,000	£1,000 £10,000 £100,000	£1,000 £10,000 £100,000	£1,000 £10,000 £100,000	£1,000 £10,000 £100,000	£1,000 £10,000 £100,000	£1,000 £10,000 £100,000	£1,000 £10,000 £100,000	£1,000 £10,000 £100,000	£1,000 £10,000 £100,000	£1,000 £10,000 £100,000
Total nominal amount	£350,000,000	£100,000,000	$286,000,000	£265,000,000	£85,000,000	£325,000,000	£100,000,000	£100,000,000	£35,000,000	£125,000,000	£125,000,000	£100,000,000	£100,000,000
Issue Price	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Currency	£	£	$	£	£	£	£	£	£	£	£	£	£
Anticipated rating - S&P/Fitch	AAA	AAA	AAA	AAA	AAA	A-	A-	A-	A-	BBB	BBB	N/A	A-
Anticipated rating - Moody's	Aaa	Aaa	Aaa	Aaa	Aaa	A3	A3	A3	A3	Baa3	Baa3	N/A	A3
Interest rate	6.015	3m£LIBOR +37.5bps Step up to 3m£LIBOR +93.75bps after 5 years	3m$LIBOR +42bps Step up to 3m$LIBOR +105bps after 7 years	3.514	3.512	6.907	3m£LIBOR +130bps Step up to 3m£LIBOR +325bps after 7 years	4.377	4.375	8.174 Conversion at 2011 to 3m£LIBOR +575	3m£LIBOR +250bps Step up to 3m£LIBOR +625bps after 7 years	3m£LIBOR +550bps Step up to 3m£LIBOR +1375 after 7 years	N/A[1]
Frequency of payment of interest	Annually	Quarterly	Quarterly	Semi-annually	Semi-annually	Annually	Quarterly	Semi-annually	Semi-annually	Annually (Quarterly after 31 March 2011)	Quarterly	Quarterly	Quarterly
Frequency of amortisation of principal	Bullet repayment	Bullet repayment	Bullet repayment	Bullet repayment	Bullet repayment	Bullet repayment	Bullet repayment	Bullet repayment	Bullet repayment	Bullet repayment	Bullet repayment	Bullet repayment	Revolver
Expected maturity	31 March 2028	31 March 2006	31 March 2008	31 March 2030	31 March 2031	31 March 2021	31 March 2008	31 March 2026	31 March 2027	31 March 2011	31 March 2008	31 March 2008	31 March 2006
Final maturity	31 March 2028	31 March 2011	31 March 2013	31 March 2030	31 March 2031	31 March 2021	31 January 2016	31 March 2026	31 March 2027	31 March 2036	31 March 2036	31 March 2036	31 March 2011
Early redemption premium	Higher of par and spens	No call year 1[2] year 2 at 101% year 3 at 100.50% after 2004 at 100%	No call year 1[2] year 2 at 101% year 3 at 100.50% after 2004 at 100%	Higher of par (after index-ation) and spens	Higher of par (after index-ation) and spens	Higher of par and spens	No call year 1[2] year 2 at 101% year 3 at 100.50% after 2004 at 100%	Higher of par (after index-ation) and spens	Higher of par (after index-ation) and spens	Higher of par and spens until 31 March 2011	No call year 1[2] year 2 at 101% year 3 at 100.50% after 2004 at 100%	No call years 1[2] and 2 year 3 at 101% year 4 at 100.50% after 2005 at 100%	N/A
Payment dates for interest and principal payments	31 March	31 March 30 June 30 Sept 31 Dec	31 March 30 June 30 Sept 31 Dec	31 March 30 Sept	31 March 30 Sept	31 March	31 March 30 June 30 Sept 31 Dec	31 March 30 Sept	31 March 30 Sept	31 March	31 March 30 June 30 Sept 31 Dec	31 March 30 June 30 Sept 31 Dec	31 March 30 June 30 Sept 31 Dec
Form at issue	Bearer form	Bearer form	Bearer form	Bearer form	Bearer form	Bearer form	Bearer form	Bearer form	Bearer form	Bearer form	Bearer form	Bearer form	Bearer form
Common Code	012831102	012831153	012831161	012831170	012906536	012831196	012831277	012831331	012906544	012831366	012831714	012831773	012831811
ISIN	XS0128311023	XS0128311536	XS0128311619	XS0128311700	XS0129065362	XS0128311965	XS0128312773	XS0128313318	XS0129065446	XS0128313664	XS0128317145	XS0128317731	XS0128318119

[1]Note: Interest rate on Class R Bonds to be determined on first re-sale by the Issuer.

[2]Note: Year 1 ends 31 March 2002; each subsequent year runs 12 months to 31 March of the following year.

Appendix B

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

(i) 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 UK 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 sewerage 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%.

(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 37 and 94 of the Act), insolvency or non-compliance with an enforcement order following breach of a licence condition.

5. Licence termination

(i) 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.

(ii) 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.

(iii) 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 (DETR). 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.*

(iv) 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.*

(v) 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.*

(vi) 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.*

* In the case of Dŵr Cymru and Dee Valley Water, these powers would be exercised by the National Assembly for Wales.

Appendix C

MBIA INSURANCE CORPORATION AND SUBSIDIARIES

CONSOLIDATED FINANCIAL STATEMENTS

AS OF DECEMBER 31, 2000 AND 1999 AND FOR THE YEARS ENDED DECEMBER 31, 2000, 1999 AND 1998.

Report of Independent Accountants

To the Board of Directors and Shareholder of
MBIA Insurance Corporation:

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income and changes in shareholder's equity and cash flows present fairly, in all material respects, the financial position of MBIA Insurance Corporation and subsidiaries as of December 31, 2000 and 1999, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2000, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion expressed above.

February 2, 2001.

MBIA INSURANCE CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

	December 31, 2000	December 31, 1999
	(Dollars in thousands except per share amounts)	
Assets		
Investments:		
Fixed-maturity securities held as available-for-sale at fair value (amortized cost $6,539,891 and $6,006,506)	$6,665,533	$5,783,979
Short-term investments, at amortized cost (which approximates fair value)	269,900	273,816
Other investments	9,663	8,425
Total investments	**6,945,096**	**6,066,220**
Cash and cash equivalents	12,541	33,702
Securities purchased under agreements to resell	330,000	205,000
Accrued investment income	106,822	93,512
Deferred acquisition costs	274,355	251,922
Prepaid reinsurance premiums	442,622	403,210
Reinsurance recoverable on unpaid losses	31,414	30,819
Goodwill (less accumulated amortization of $61,784 and $56,906)	81,196	86,075
Property and equipment, at cost (less accumulated depreciation of $38,309 and $31,104)	117,338	111,549
Receivable for investments sold	2,497	2,882
Other assets	105,846	161,082
Total Assets	**$8,449,727**	**$7,445,973**
Liabilities and Shareholders' Equity		
Liabilities:		
Deferred premium revenue	$2,397,578	$2,310,758
Loss and loss adjustment expense reserves	499,279	467,279
Securities sold under agreements to repurchase	330,000	205,000
Deferred income taxes	253,363	79,895
Deferred fee revenue	26,138	28,478
Payable for investments purchased	2,334	18,948
Other liabilities	133,429	107,988
Total Liabilities	**$3,642,121**	**$3,218,346**
Shareholders' Equity:		
Common stock, par value $150 per share; authorized, issued and outstanding – 100,000 shares	15,000	15,000
Additional paid-in capital	1,540,071	1,514,014
Retained earnings	3,191,536	2,858,210
Accumulated other comprehensive income (loss), net of deferred income tax provision (benefit) of $43,910 and $(77,942)	60,999	(159,597)
Total Shareholders' Equity	**4,807,606**	**4,227,627**
Total Liabilities Shareholders' Equity	**$8,449,727**	**$7,445,973**

The accompanying notes are an integral part of the consolidated financial statements.

MBIA INSURANCE CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

	Years ended December 31,		
	2000	1999	1998
	(Dollars in thousands)		
Revenues:			
Gross premiums written	$687,408	624,871	$725,269
Ceded premiums	(189,316)	(171,256)	(149,280)
Net premiums written	498,092	453,615	575,989
Increase in deferred premium revenue	(51,739)	(10,819)	(166,182)
Premiums earned (net of ceded premiums of $147,249 $119,879, and $92,802)	446,353	442,796	409,807
Net investment income	392,078	358,836	326,391
Net realized gains	24,721	32,680	29,891
Advisory fees	24,027	22,885	23,964
Other	1,564	—	713
Total revenues	**888,743**	**857,197**	**790,766**
Expenses:			
Losses and loss adjustment	51,291	198,454	33,661
Policy acquisition costs, net	35,976	36,700	33,168
Operating	80,376	76,599	65,445
Total expenses	**167,643**	**311,753**	**132,274**
Income before income taxes	721,100	545,444	658,492
Provision for income taxes	190,474	73,456	134,593
Net income	**$530,626**	**$471,988**	**$523,899**

The accompanying notes are an integral part of the consolidated financial statements.

MBIA INSURANCE CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDER'S EQUITY

For the years ended December 31, 2000, 1999, and 1998

	Common Stock		Additional Paid-in Capital	Retained earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholder's Equity
	Shares	Amount				
	(In thousands except per share amounts)					
Balance, January 1, 1998	100,000	$15,000	$1,139,949	$2,042,323	$166,587	$3,363,859
Comprehensive income:						
Net income	—	—	—	523,899	—	523,899
Other comprehensive income:						
Change in unrealized appreciation of investments net of change in deferred income taxes of $17,867	—	—	—	—	34,084	34,084
Change in foreign currency translation	—	—	—	—	4,419	4,419
Other comprehensive income						38,503
Comprehensive income						562,402
Capital contribution from MBIA Inc.	—	—	324,915	—	—	324,915
Tax reduction related to tax sharing agreement with MBIA Inc.	—	—	26,169	—	—	26,169
Balance, December 31, 1998	100,000	15,000	1,491,033	2,566,222	205,090	4,277,345
Comprehensive income:						
Net income	—	—	—	471,988	—	471,988
Other comprehensive income (loss):						
Change in unrealized appreciation of investments net of change in deferred income taxes of $(190,225)	—	—	—	—	(354,231)	(354,231)
Change in foreign currency translation	—	—	—	—	(10,456)	(10,456)
Other comprehensive income (loss)						(364,687)
Comprehensive income						107,301
Dividends declared (per common share $1,800.00)	—	—	—	(180,000)	—	(180,000)
Tax reduction related to tax sharing agreement with MBIA Inc.	—	—	22,981	—	—	22,981
Balance, December 31, 1999	100,000	15,000	1,514,014	2,858,210	($159,597)	4,227,627
Comprehensive income:						
Net income	—	—	—	530,626	—	530,626
Other comprehensive income:						
Change in unrealized appreciation of investments net of change in deferred income taxes of $121,852	—	—	—	—	226,480	226,480
Change in foreign currency translation	—	—	—	—	(5,884)	(5,884)
Other comprehensive income						220,596
Comprehensive income						751,222
Dividends declared (per common share $1,973.00)	—	—	—	(197,300)	—	(197,300)
Tax reduction related to tax sharing agreement with MBIA Inc.	—	—	26,057	—	—	26,057
Balance, December 31, 2000	100,000	$15,000	$1,540,071	$3,191,536	$60,999	$4,807,606

	2000	1999	1998
Disclosure of reclassification amount:			
Unrealized (depreciation) appreciation of investments arising during the period, net of taxes	$228,513	$(304,809)	$53,415
Reclassification of adjustment, net of taxes	(2,033)	(49,422)	(19,331)
Net unrealized appreciation, net of taxes	$226,480	$(354,231)	$34,084

The accompanying notes are an integral part of the consolidated financial statements.

MBIA INSURANCE CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years ended December 31,		
	2000	1999	1998
	(Dollars in thousands)		
Cash flows from operating activities:			
Net income	$ 530,626	$ 471,988	$ 523,899
Adjustments to reconcile net income to net cash provided by operating activities:			
Increase in accrued investment income	(13,310)	(2,273)	(12,638)
Increase in deferred acquisition costs	(22,433)	(21,837)	(75,985)
Increase in prepaid reinsurance premiums	(39,412)	(50,511)	(99,806)
Increase in deferred premium revenue	91,151	61,330	265,983
Increase in loss and loss adjustment expense reserves, net	31,405	166,346	191,242
Depreciation	7,205	7,803	5,626
Amortization of goodwill	4,879	4,875	4,879
Amortization of bond discount, net	(16,756)	(18,642)	(15,831)
Net realized gains on sale of investments	(24,721)	(32,680)	(29,891)
Deferred income tax provision (benefit)	51,597	(33,170)	21,856
Other, net	94,282	(84,803)	43,593
Total adjustments to net income	163,887	(3,562)	299,028
Net cash provided by operating activities	694,513	468,426	822,927
Cash flows from investing activities:			
Purchase of fixed-maturity securities, net of payable for investments purchased	(2,984,404)	(2,001,636)	(2,800,008)
Sale of fixed-maturity securities, net of receivable for investments sold	2,183,222	1,376,747	1,086,973
Redemption of fixed-maturity securities, net of receivable for investments redeemed	282,541	288,710	745,516
Sale (purchase) of short-term investments, net	12,947	114,096	(158,339)
Sale (purchase) of other investments, net	331	8,222	(527)
Capital expenditures, net of disposals	(13,011)	(47,409)	(18,894)
Net cash used by investing activities	(518,374)	(261,270)	(1,145,279)
Cash flows from financing activities:			
Capital contribution from MBIA Inc.	—	—	324,915
Dividends paid	(197,300)	(180,000)	—
Net cash (used) provided by financing activities	(197,300)	(180,000)	324,915
Net (decrease) increase in cash and cash equivalents	(21,161)	27,156	2,563
Cash and cash equivalents – beginning of year	33,702	6,546	3,983
Cash and cash equivalents – end of year	$ 12,541	$ 33,702	$ 6,546
Supplemental cash flow disclosures:			
Income taxes paid	$ 83,020	$ 125,176	$ 105,451

The accompanying notes are an integral part of the consolidated financial statements.

MBIA INSURANCE CORPORATION AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Business and Organization

MBIA Insurance Corporation (MBIA Corp.), formerly known as Municipal Bond Investors Assurance Corporation, is a wholly owned subsidiary of MBIA Inc. MBIA Inc. was incorporated in Connecticut on November 12, 1986 as a licensed insurer and, through a series of transactions during December 1986, became the successor to the business of the Municipal Bond Insurance Association (the Association), a voluntary unincorporated association of insurers writing municipal bond and note insurance as agent for the member insurance companies.

Effective December 31, 1989, MBIA Inc. acquired for $288 million all of the outstanding stock of Bond Investors Group, Inc. (BIG), the parent company of Bond Investors Guaranty Insurance Company (BIG Ins.), which was subsequently renamed MBIA Insurance Corp. of Illinois (MBIA Illinois).

In January 1990, MBIA Illinois ceded its portfolio of net insured obligations to MBIA Corp. in exchange for cash and investments equal to its unearned premium reserve of $153 million. Subsequent to this cession, MBIA Inc. contributed the common stock of BIG to MBIA Corp. resulting in additional paid-in capital of $200 million. The insured portfolio acquired from BIG Ins. consists of municipal obligations with risk characteristics similar to those insured by MBIA Corp. On December 31, 1990, BIG was merged into MBIA Illinois.

Also in 1990, MBIA Inc. formed MBIA Assurance S.A. (MBIA Assurance), a wholly owned French subsidiary, to write financial guarantee insurance in the international community. MBIA Assurance provides insurance for public infrastructure financings, structured finance transactions and certain obligations of financial institutions. The stock of MBIA Assurance was contributed to MBIA Corp. in 1991 resulting in additional paid-in capital of $6 million. Pursuant to a reinsurance agreement with MBIA Corp., a substantial amount of the risks insured by MBIA Assurance is reinsured by MBIA Corp.

In 1993, MBIA Inc. formed a wholly owned subsidiary, MBIA Investment Management Corp. (IMC). IMC provides guaranteed investment agreements to states, municipalities and municipal authorities that are guaranteed as to principal and interest. MBIA Corp. insures IMC's outstanding investment agreement liabilities.

In 1994, MBIA Inc. formed a wholly owned subsidiary, MBIA Securities Corp., which was subsequently renamed MBIA Capital Management Corp. (CMC). CMC provides fixed-income investment management services for MBIA Inc. and its affiliates and third party institutional clients. In 1995, portfolio management for a portion of MBIA Corp.'s insurance related investment portfolio was transferred to CMC; the management of the balance of this portfolio was transferred in January 1996.

On February 17, 1998 MBIA Inc. and CapMAC Holdings Inc. (CapMAC) consummated a merger. Under the terms of the merger, CapMAC shareholders received 0.4675 of a share of MBIA Inc. common stock for each CapMAC share, for a total of 8,102,255 newly issued shares of MBIA Inc. common stock, the value of which was $536 million. On April 1, 1998, MBIA Corp. assumed the net insured obligations of Capital Markets Assurance Corporation (CMAC) in exchange for investments equal to $176.1 million. The cession of the deferred premium revenue (net of prepaid reinsurance premiums) in the amount of $68.2 million has been reflected as a component of gross premium written in the second quarter of 1998. Subsequent to the cession MBIA Inc. contributed the common stock of CMAC to MBIA Corp. resulting in additional paid-in capital of $324.9 million.

MBIA Corp. has one business segment – Financial Guarantee Insurance. The financial guarantee business provides an unconditional and irrevocable guarantee of the payment of principal and interest on insured obligations when due.

2. Significant Accounting Policies

The consolidated financial statements have been prepared on the basis of accounting principles generally accepted in the United States of America (GAAP). The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant accounting policies are as follows:

Consolidation

The consolidated financial statements include the accounts of MBIA Corp. and its wholly owned subsidiaries. All significant intercompany balances have been eliminated. Certain amounts have been reclassified in prior years' financial statements to conform to the current presentation.

Investments

MBIA Corp.'s investment portfolio is considered available-for-sale and is reported in the financial statements at fair value, with unrealized gains and losses, net of deferred taxes, reflected as a separate component of shareholder's equity.

Bond discounts and premiums are amortized using the effective-yield method over the remaining term of the securities. For pre-refunded bonds the remaining term is determined based on the contractual refunding date. Short-term investments are carried at amortized cost, which approximates fair value, and include all fixed-maturity securities with a remaining effective term to maturity of less than one year. Investment income is recorded as earned. Realized gains or losses on the sale of investments are determined by specific identification and are included as a separate component of revenues.

Other investments include MBIA Corp.'s interest in equity oriented investments. In addition, MBIA Corp. records its share of the unrealized gains and losses on these investments, net of applicable deferred income taxes, as a separate component of shareholder's equity.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand and demand deposits with banks.

Securities purchased under agreements to resell and securities sold under agreements to repurchase

Securities purchased under agreements to resell and securities sold under agreements to repurchase are accounted for as collateralized transactions and are recorded at principal or contract value. It is MBIA Corp.'s policy to take possession of securities purchased under agreements to resell. These contracts are primarily entered into to obtain securities that are repledged as part of MBIA Corp.'s collateralized municipal investment and repurchase activity and are only transacted with high-quality dealer firms.

MBIA Corp. minimizes the credit risk that counterparties to transactions might be unable to fulfill their contractual obligations by monitoring customer credit exposure and collateral value and requiring additional collateral to be deposited with MBIA Corp. when deemed necessary.

Policy Acquisition Costs

Policy acquisition costs include only those expenses that relate primarily to, and vary with, premium production. For business produced directly by MBIA Corp., such costs include compensation of employees involved in underwriting and policy issuance functions, certain rating agency fees, state premium taxes and certain other underwriting expenses, reduced by ceding commission income on premiums ceded to reinsurers. Policy acquisition costs are deferred and amortized over the period in which the related premiums are earned.

Premium Revenue Recognition

Upfront premiums are earned pro rata over the period of risk. Premiums are allocated to each bond maturity based on par amount and are earned on a straight-line basis over the term of each maturity. Installment premiums are earned over each installment period – generally one year or less. When an insured issue is retired early, is called by the issuer, or is in substance paid in advance through a refunding accomplished by placing U.S. Government securities in escrow, the remaining deferred premium revenue is earned at that time, since there is no longer risk to MBIA Corp. Accordingly, deferred premium revenue represents the portion of premiums written that is applicable to the unexpired risk of insured bonds and notes.

Advisory Fee Revenue Recognition

MBIA Corp. collects advisory fees for services rendered in connection with advising clients as to the most appropriate structure to use for a given insured transaction. In addition, the company earns advisory fees in connection with its administration of certain third-party-owned conduits. Most fees are deferred and earned pro-rata over the life of the underlying transactions. Certain fees, however, are

earned in the quarter they are collected and include administrative fees for transactions where the fee is collected on a periodic installment basis and fees for transactions which terminate prior to the expected maturity date.

Goodwill

Goodwill represents the excess of the cost of acquisitions over the tangible net assets acquired. Goodwill attributed to the acquisition of MBIA Corp. is amortized by the straight-line method over 25 years. Goodwill attributed to the acquisition of MBIA Illinois is amortized according to the recognition of future profits from its deferred premium revenue and installment premiums, except for a minor portion attributed to state licenses, which is amortized by the straight-line method over 25 years.

Property and Equipment

Property and equipment consists of MBIA Corp.'s headquarters, furniture, fixtures and equipment, which are recorded at cost and are depreciated on the straight-line method over their estimated service lives ranging from 3 to 31 years. Maintenance and repairs are charged to expense as incurred.

Losses and Loss Adjustment Expenses

Loss and loss adjustment expense (LAE) reserves are established in an amount equal to MBIA Corp.'s estimate of identified or case basis reserves and unallocated losses, including costs of settlement, on the obligations it has insured.

Case basis reserves are established when specific insured issues are identified as currently or likely to be in default. Such a reserve is based on the present value of the expected loss and LAE payments, net of recoveries, under salvage and subrogation rights, based on a discount rate of 6.12%. The total reserve is calculated by applying a loss factor, determined based on an independent rating agency study of issuer defaults, to net debt service written. When a case basis reserve is recorded, a corresponding reduction is made to the unallocated reserve.

Management of MBIA Corp. periodically evaluates its estimates for losses and LAE and any resulting adjustments are reflected in current earnings. Management believes that the reserves are adequate to cover the ultimate net cost of claims, but the reserves are necessarily based on estimates, and there can be no assurance that the ultimate liability will not exceed such estimates.

In 2000 and 1999, MBIA Corp. reviewed its loss reserving methodology. The reviews included an analysis of loss reserve factors based on the latest available industry data. They included the analysis of historical default and recovery experience for the relevant sectors of the fixed-income market. Also factored in was the changing mix of our book of business. The 1999 review resulted in an increase in MBIA Corp.'s current loss reserving factors.

Derivatives

Effective January 1, 2001 the company will adopt Statement of Financial Accounting Standards (SFAS) 133, Accounting for Derivative Instruments and Hedging Activities. See footnote 4 for an explanation of the impact the adoption of this statement will have on MBIA Corp.'s financial statements.

Income Taxes

MBIA Corp. is included in the consolidated tax return of MBIA Inc. The tax provision for MBIA Corp. for financial reporting purposes is determined on a stand alone basis. Any benefit derived by MBIA Corp. as a result of the tax sharing agreement with MBIA Inc. and its subsidiaries is reflected directly in shareholder's equity for financial reporting purposes.

Deferred income taxes are provided with respect to the temporary differences between the tax bases of assets and liabilities and the reported amounts in the financial statements that will result in deductible or taxable amounts in future years when the reported amount of the asset or liability is recovered or settled. Such temporary differences relate principally to premium revenue recognition, deferred acquisition costs, unrealized appreciation or depreciation of investments and the contingency reserve.

The Internal Revenue Code permits companies writing financial guarantee insurance to deduct from taxable income amounts added to the statutory contingency reserve, subject to certain limitations. The tax benefits obtained from such deductions must be invested in non-interest-bearing U.S. Government tax and loss bonds. MBIA Corp. records purchases of tax and loss bonds as payments of

federal income taxes. The amounts deducted must be restored to taxable income when the contingency reserve is released, at which time MBIA Corp. may present the tax and loss bonds for redemption to satisfy the additional tax liability.

Foreign Currency Translation

Assets and liabilities denominated in foreign currencies are translated at year-end exchange rates. Operating results are translated at average rates of exchange prevailing during the year. Unrealized gains or losses resulting from translation are included as a separate component of shareholder's equity. Gains and losses resulting from transactions in foreign currencies are recorded in current income.

3. Statutory Accounting Practices

The financial statements have been prepared on the basis of GAAP, which differs in certain respects from the statutory accounting practices prescribed or permitted by the insurance regulatory authorities. Statutory accounting practices differ from GAAP in the following respects:

- upfront premiums are earned on a basis proportionate to the scheduled periodic maturity of principal and payment of interest (''debt service'') to the original total principal and interest insured;
- acquisition costs are charged to operations as incurred rather than deferred and amortized as the related premiums are earned;
- a contingency reserve is computed on the basis of statutory requirements, and reserves for case basis losses and LAE are established, at present value, for specific insured issues that are identified as currently or likely to be in default. Under GAAP, reserves are established based on MBIA Corp.'s reasonable estimate of the identified and unallocated losses and LAE on the insured obligations it has written;
- federal income taxes are only provided on taxable income for which income taxes are currently payable, while under GAAP, deferred income taxes are provided with respect to temporary differences;
- fixed-maturity securities are reported at amortized cost rather than fair value;
- tax and loss bonds purchased are reflected as admitted assets as well as payments of income taxes; and
- certain assets designated as ''non-admitted assets'' are charged directly against surplus but are reflected as assets under GAAP.

The following is a reconciliation of consolidated shareholder's equity presented on a GAAP basis to statutory capital and surplus for MBIA Corp. and its subsidiaries:

	As of December 31,	
	2000	1999
	(In thousands)	
GAAP shareholder's equity	$4,807,606	$4,227,627
Premium revenue recognition	(535,920)	(491,766)
Deferral of acquisition costs	(274,354)	(251,922)
Unrealized (gains) losses	(125,529)	222,803
Contingency reserve	(2,123,403)	(1,738,730)
Loss and loss adjustment expense reserves	258,706	232,004
Deferred income taxes	253,363	79,895
Tax and loss bonds	202,195	219,195
Goodwill	(81,196)	(86,075)
Other	201	336
Statutory capital and surplus	$2,381,669	$2,413,367

Aggregate net income of MBIA Corp. and its subsidiaries determined in accordance with statutory accounting practices for the years ended December 31, 2000, 1999 and 1998 was $543.9 million, $521.8 million and $498.2 million, respectively.

In 1998, the National Association of Insurance Commissioners (NAIC) adopted the Codification of Statutory Accounting Principles guidance, which replaces the current Accounting Practices and Procedures manuals as the NAIC's primary guidance on statutory accounting effective as of January 1, 2001. The Codification provides guidance for areas where statutory accounting has been silent and changes current statutory accounting in some areas; e.g. deferred income taxes are recorded.

The New York State Insurance Department has adopted the Codification guidance, effective January 1, 2001. The New York State Insurance Department has not adopted the Codification rules on certain accounting issues; e.g. deferred income taxes and goodwill. The effect of adoption on MBIA Corp.'s statutory surplus is expected to be immaterial to MBIA Corp.

4. Recent Accounting Pronouncement

In June 1998, the Financial Accounting Standards Board (FASB) issued SFAS 133, ''Accounting for Derivative Instruments and Hedging Activities which is effective for the company as of January 1, 2001. SFAS 133 requires that all derivative instruments be recorded on the balance sheet at their fair value. Changes in the fair value of derivatives will be recorded each period in current earnings or other comprehensive income, depending on whether a derivative is designated as part of a hedge, and if so, the use and type of the hedge.

MBIA Corp. has entered into derivative transactions that do not qualify for the financial guarantee scope exception under SFAS 133 and, therefore, must be stated at fair value. The Insurance segment, which represents the majority of the company's derivative exposure and mark to market as of January 1, 2001, has insured derivatives primarily consisting of credit default swaps.

Adoption of SFAS 133, on January 1, 2001 will result in MBIA Corp.'s after-tax reductions in net income of approximately $10.7 million. In addition, the company will increase its assets by approximately $36.2 million and liabilities by approximately $46.9 million on an after-tax basis.

5. Premiums Earned from Refunded and Called Bonds

Premiums earned include $34.0 million, $64.2 million and $68.4 million for 2000, 1999 and 1998, respectively, related to refunded and called bonds.

6. Investments

MBIA Corp.'s investment objective is to optimize long-term, after-tax returns while emphasizing the preservation of capital through maintenance of high-quality investments with adequate liquidity. MBIA Corp.'s investment policies limit the amount of credit exposure to any one issuer. The fixed-maturity portfolio is comprised of high-quality (average rating Double-A) taxable and tax-exempt investments of diversified maturities.

The following tables set forth the amortized cost and fair value of the fixed-maturities and short-term investments included in the consolidated investment portfolio of MBIA Corp. as of December 31, 2000 and 1999:

	Amortized Cost	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
		(In thousands)		
December 31, 2000				
Taxable bonds United States				
Treasury and Government Agency	$ 148,911	$ 2,364	$ (690)	$ 150,585
Corporate and other obligations	2,126,124	32,188	(35,383)	2,122,929
Mortgage-backed	779,780	14,785	(3,252)	791,313
Tax-exempt bonds State and municipal obligations	3,754,976	127,916	(12,286)	3,870,606
Total	$ 6,809,791	$ 177,253	$ (51,611)	$ 6,935,433

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
		(In thousands)		
December 31, 1999				
Taxable bonds				
United States Treasury and Government Agency	$ 29,913	$ 116	$ (2,926)	$ 27,103
Corporate and other obligations	1,817,867	2,227	(79,673)	1,740,421
Mortgage-backed	790,748	3,874	(21,436)	773,186
Tax-exempt bonds State and municipal obligations	3,641,794	50,334	(175,043)	3,517,085
Total	$ 6,280,322	$ 56,551	$ (279,078)	$ 6,057,795

Fixed-maturity investments carried at fair value of $11.7 million and $11.6 million as of December 31, 2000 and 1999, respectively, were on deposit with various regulatory authorities to comply with insurance laws.

The following table sets forth the distribution by expected maturity of the fixed-maturities and short-term investments at amortized cost and fair value at December 31, 2000. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations.

	Amortized Cost	Fair Value
	(In thousands)	
Within 1 year	$ 252,609	$ 252,609
Beyond 1 year but within 5 years	847,492	858,562
Beyond 5 years but within 10 years	1,118,948	1,134,494
Beyond 10 years but within 15 years	1,128,016	1,170,286
Beyond 15 years but within 20 years	1,254,464	1,293,067
Beyond 20 years	1,428,482	1,435,101
	6,030,011	6,144,119
Mortgage-backed	779,780	791,314
Total fixed-maturities and short-term investments	$6,809,791	$6,935,433

7. Investment Income and Gains and Losses

Investment income consists of:

	Years ended December 31,		
	2000	1999	1998
	(In thousands)		
Fixed-maturities	$388,134	$357,702	$326,820
Short-term investments	10,410	7,221	5,311
Other investments	(80)	24	16
Gross investment income	398,464	364,947	332,147
Investment expenses	6,386	6,111	5,756
Net investment income	392,078	358,836	326,391
Net realized gains (losses):			
Fixed-maturities:			
Gains	42,765	47,244	32,211
Losses	(19,516)	(16,793)	(3,149)
Net	23,249	30,451	29,062
Other investments:			
Gains	1,853	2,229	829
Losses	(380)	—	—
Net	1,473	2,229	829
Total net realized gains	24,722	32,680	29,891
Total investment income	$416,800	$391,516	$356,282

Net unrealized gains (losses) consist of:

	As of December 31,	
	2000	1999
	(In thousands)	
Fixed-maturities:		
Gains	$ 177,253	$ 56,551
Losses	(51,611)	(279,078)
Net	125,642	(222,527)
Other investments:		
Gains	—	—
Losses	(113)	(276)
Net	(113)	(276)
Total	125,529	(222,803)
Deferred income tax provision (benefit)	43,910	(77,942)
Unrealized gains (losses), net	$ 81,619	$(144,861)

The deferred income tax provision (benefit) relate primarily to unrealized gains and losses on MBIA Corp.'s fixed-maturity investments, which are reflected in shareholder's equity.

The change in net unrealized gains (losses) consists of:

	Years ended December 31,		
	2000	1999	1998
		(In thousands)	
Fixed-maturities	$348,169	$(541,520)	$52,267
Other investments	163	(2,936)	(316)
Total	348,332	(544,456)	51,951
Deferred income taxes	121,852	(190,225)	17,867
Unrealized gains (losses), net	$226,480	$(354,231)	$34,084

8. Income Taxes

The provision for income taxes is composed of:

	Years ended December 31,		
	2000	1999	1998
		(In thousands)	
Current	$138,877	$106,626	$112,737
Deferred	51,597	(33,170)	21,856
Total	$190,474	$ 73,456	$134,593

The provision for income taxes gives effect to permanent differences between financial and taxable income. Accordingly, MBIA Corp.'s effective income tax rate differs from the statutory rate on ordinary income. The reasons for MBIA Corp.'s lower effective tax rates are as follows:

	Years ended December 31,		
	2000	1999	1998
		(per cent.)	
Income taxes computed on pre-tax financial income at statutory rates	35.0%	35.0%	35.0%
Increase (reduction) in taxes resulting from:			
Tax-exempt interest	(8.5)	(11.4)	(9.1)
Amortization of goodwill	0.2	0.3	0.3
Other	(0.3)	(10.4)	(5.8)
Provision for income taxes	26.4%	13.5%	20.4%

The 1999 effective tax rate includes a reduction of 10.4% pertaining to the loss reserve strengthening.

MBIA Corp. recognizes deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements or tax returns. Deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. The effect on tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

The tax effects of temporary differences that give rise to deferred tax assets and liabilities at December 31, 2000 and 1999 are presented below:

	2000	1999
	(In thousands)	
Deferred tax assets:		
Tax and loss bonds	$199,607	$206,999
Alternative minimum tax credit carryforward	11,381	65,404
Loss and loss adjustment expense reserves	88,396	79,051
Unrealized losses	—	77,942
Other	36,319	45,668
Total gross deferred tax assets	335,703	475,064
Deferred tax liabilities:		
Contingency reserve	324,305	330,125
Deferred premium revenue	105,731	110,785
Deferred acquisition costs	96,024	88,173
Unrealized gains	43,910	—
Contingent commissions	620	408
Other	18,476	25,468
Total gross deferred tax liabilities	589,066	554,959
Net deferred tax liability	$253,363	$79,895

MBIA Corp. believes that no valuation allowance is necessary in connection with the deferred tax assets.

9. Dividends and Capital Requirements

Under New York state insurance law, MBIA Corp. and CMAC may pay dividends only from earned surplus subject to the maintenance of a minimum capital requirement. The dividends in any 12-month period may not exceed the lesser of 10% of its policyholders' surplus (total capital and surplus) as shown on its last filed statutory-basis financial statements, or of adjusted net investment income, as defined, for such 12-month period, without prior approval of the superintendent of the New York State Insurance Department.

In accordance with such restrictions on the amount of dividends which can be paid in any 12-month period, MBIA Corp. had in excess of $40 million available for the payment of dividends as of December 31, 2000. MBIA Corp. declared and paid dividends of $197.3 million and $180.0 million to MBIA Inc. in 2000 and 1999, respectively. CMAC declared and paid dividends of $4.5 million and $1.0 million to its parent MBIA Corp in 2000 and 1999, respectively.

Under Illinois Insurance Law, MBIA Illinois may pay a dividend from unassigned surplus, and the dividends in any 12-month period may not exceed the greater of 10% of policyholders' surplus (total capital and surplus) at the end of the preceding calendar year, or the net income of the preceding calendar year without prior approval of the Illinois State Insurance Department.

In accordance with such restrictions on the amount of dividends that can be paid in any 12-month period, MBIA Illinois had in excess of $100 thousand available for the payment of dividends as of December 31, 2000. MBIA Illinois declared and paid dividends of $17.5 million and $1.0 million to its parent MBIA Corp. in 2000 and 1999, respectively.

The insurance departments of New York state and certain other statutory insurance regulatory authorities and the agencies that rate the bonds insured by MBIA Corp. and its subsidiaries have various requirements relating to the maintenance of certain minimum ratios of statutory capital and reserves to net insurance in force. MBIA Corp. and its subsidiaries were in compliance with these requirements as of December 31, 2000.

10. Lines of Credit

MBIA Corp. has a standby line of credit commitment in the amount of $900 million with a group of major Triple-A-rated banks to provide loans to MBIA Corp. if it incurs cumulative losses (net of any recoveries) from October 27, 2000 in excess of the greater of $900 million or 5.60% of average annual debt service. The obligation to repay loans made under this agreement is a limited recourse obligation payable solely from, and collateralized by, a pledge of recoveries realized on defaulted insured obligations including certain installment premiums and other collateral. This commitment has a seven-year term expiring on October 31, 2007, and contains an annual renewal provision subject to approval by the bank group. MBIA Corp. also maintains stop-loss reinsurance coverage of $175 million in excess of incurred losses of $762 million.

MBIA Corp. and MBIA Inc. maintain bank liquidity facilities totaling $650 million. As of December 31, 2000, there were no borrowings outstanding under these agreements.

11. Net Insurance In Force

MBIA Corp. guarantees the timely payment of principal and interest on municipal, asset-/mortgage-backed and other non-municipal securities. MBIA Corp.'s ultimate exposure to credit loss in the event of nonperformance by the insured is represented by the insurance in force as set forth below.

As of December 31, 2000, insurance in force, net of cessions to reinsurers, had a range of maturity of 1-49 years diversified among 35,691 outstanding policies. The distribution of net insurance in force by geographic location, including $5.3 billion and $4.5 billion relating to IMC's municipal investment agreements guaranteed by MBIA Corp. in 2000 and 1999, respectively, is set forth in the following table:

	As of December 31,			
	2000		1999	
Geographic Location	**Net Insurance In Force**	**% of Net Insurance In Force**	**Net Insurance In Force**	**% of Net Insurance In Force**
	($ in billions)	%	*($ in billions)*	%
Domestic:				
California	$ 80.0	11.6%	$ 76.6	12.0%
New York	76.4	11.1	75.8	11.8
Florida	35.7	5.2	36.3	5.7
Texas	26.7	3.9	26.6	4.1
New Jersey	26.0	3.8	24.4	3.8
Pennsylvania	24.5	3.6	25.8	4.0
Illinois	22.6	3.3	22.1	3.5
Massachusetts	20.5	3.0	19.2	3.0
Michigan	14.8	2.1	15.0	2.3
Ohio	13.5	2.0	13.1	2.1
Subtotal	340.7	49.6	334.9	52.3
Nationally Diversified	117.2	17.1	97.1	15.2
Other states	180.4	26.3	175.0	27.3
Total domestic	638.3	93.0	607.0	94.8
International	47.9	7.0	33.4	5.2
Total	$686.2	100.0%	$640.4	100.0%

The insurance policies issued by MBIA Corp. are unconditional commitments to guarantee timely payment on the bonds and notes to bondholders. The creditworthiness of each insured issue is evaluated prior to the issuance of insurance and each insured issue must comply with MBIA Corp.'s underwriting guidelines. Further, the payments to be made by the issuer on the bonds or notes may be

backed by a pledge of revenues, reserve funds, letters of credit, investment contracts or collateral in the form of mortgages or other assets. The right to such money or collateral would typically become MBIA Corp.'s upon the payment of a claim by MBIA Corp.

Under certain structured asset-backed transactions, a pool of assets covering at least 100% of the principal amount guaranteed under its insurance contract is sold or pledged to a special-purpose bankruptcy remote entity. MBIA Corp.'s primary risk from such insurance contracts is the impairment of cash flows due to delinquency or loss on the underlying assets. MBIA Corp. therefore evaluates all the factors affecting past and future asset performance by studying historical data on losses, delinquencies and recoveries of the underlying assets. Each transaction is reviewed to ensure that an appropriate legal structure is used to protect against the bankruptcy risk of the originator of the assets. Along with the legal structure, an additional level of first-loss protection is also created to protect against losses due to credit or dilution. This first level of loss protection is usually available from reserve funds, excess cash flows, overcollateralization or recourse to a third party. The level of first-loss protection depends upon the historical losses and dilution of the underlying assets, but is typically several times the normal historical loss experience for the underlying type of assets. The distribution of net insurance in force by type of bond is set forth in the following table:

Type of Bond	As of December 31, 2000 Net Insurance In Force	2000 % of Net Insurance In Force	1999 Net Insurance In Force	1999 % of Net Insurance In Force
	($ in billions)	%	*($ in billions)*	%
Domestic				
Public Finance:				
General obligation	$152.7	22.3%	$147.5	23.0%
Utilities	77.9	11.4	78.1	12.2
Health care	68.3	10.0	70.6	11.1
Special revenue	61.4	8.9	52.5	8.2
Transportation	48.7	7.1	45.5	7.1
Investor owned utilities	37.2	5.4	33.0	5.2
Higher education	28.8	4.2	27.1	4.2
Housing	24.4	3.5	23.3	3.6
Total public finance	499.4	72.8	477.6	74.6
Structured finance:				
Mortgage-backed:				
Home equity	33.8	4.9	43.2	6.7
Other	20.5	3.0	19.8	3.1
First mortgage	11.3	1.6	13.1	2.0
Asset-backed:				
Other	23.3	3.4	16.9	2.6
Auto	14.7	2.2	8.7	1.4
Leasing	5.3	0.8	6.3	1.0
Pooled corp. obligations and other	24.2	3.5	15.2	2.4
Financial risk	5.8	0.8	6.2	1.0
Total structured finance	138.9	20.2	129.4	20.2
Total domestic	638.3	93.0	607.0	94.8
International Infrastructure:				
Sovereign	2.7	0.4	2.1	0.3
Utilities	2.5	0.4	1.6	0.2
Transportation	1.6	0.2	1.1	0.2
Investor owned utilities	1.4	0.2	1.1	0.2
Sub-sovereign	1.0	0.1	1.2	0.2
Health care	0.6	0.1	0.7	0.1
Housing	0.5	0.1	0.6	0.1
Higher education	0.1	—	0.1	—
Total infrastructure	10.4	1.5	8.5	1.3
Structured finance:				
Pooled corp. obligation and other	27.9	4.0	17.6	2.8
Mortgage-backed	4.5	0.7	1.7	0.2
Financial risk	3.4	0.5	3.7	0.6
Asset-backed	1.7	0.3	1.9	0.3
Total structured finance	37.5	5.5	24.9	3.9
Total international	47.9	7.0	33.4	5.2
Total	$686.2	100.0%	$640.4	100.0%

12. Reinsurance

MBIA Corp. reinsures exposure with other insurance companies under various treaty and facultative reinsurance contracts, both on a pro rata and excess of loss basis. In the event that any or all of the reinsurers were unable to meet their obligations, MBIA Corp. would be liable for such defaulted amounts.

Amounts deducted from gross insurance in force for reinsurance ceded by MBIA Corp. and its subsidiaries were $143.3 billion and $129.0 billion, at December 31, 2000 and 1999, respectively. The distribution of ceded insurance in force by geographic location is set forth in the following table:

	As of December 31,			
	2000		1999	
Geographic Location	**Ceded Insurance In Force**	**% of Ceded Insurance In Force**	**Ceded Insurance In Force**	**% of Ceded Insurance In Force Domestic:**
	($ in billions)	%	*($ in billions)*	%
Domestic:				
California	$ 17.9	12.5	$ 17.6	13.6%
New York	13.7	9.5	14.0	10.9
New Jersey	6.9	4.8	5.5	4.3
Texas	5.3	3.7	5.5	4.2
Florida	4.7	3.3	5.0	3.9
Massachusetts	4.2	3.0	4.1	3.2
Pennsylvania	4.2	2.9	4.6	3.5
Colorado	3.8	2.7	2.4	1.9
Puerto Rico	3.7	2.6	3.2	2.5
Illinois	3.6	2.5	3.4	2.6
Subtotal	68.0	47.5	65.3	50.6
Nationally diversified	18.8	13.1	14.4	11.2
Other states	29.2	20.3	28.0	21.7
Total domestic	116.0	80.9	107.7	83.5
International	27.3	19.1	21.3	16.5
Total	$143.3	100.0%	$129.0	100.0%

The distribution of ceded insurance in force by type of bond is set forth in the following table:

	As of December 31,			
	2000		1999	
Type of Bond	**Ceded Insurance In Force**	**% of Ceded Insurance In Force**	**Ceded Insurance In Force**	**% of Ceded Insurance In Force**
	($ in billions)	*%*	*($ in billions)*	*%*
Domestic:				
Public Finance:				
General obligation	$19.8	13.9%	$18.8	14.6%
Transportation	18.4	12.8	14.7	11.4
Utilities	17.1	11.9	17.2	13.3
Health care	15.3	10.7	15.7	12.2
Special revenue	9.4	6.6	8.8	6.8
Investor owned utilities	6.1	4.2	5.7	4.5
Housing	2.8	1.9	2.7	2.1
Higher education	2.4	1.7	2.1	1.6
Total public finance	91.3	63.7	85.7	66.5
Structured finance:				
Mortgage-backed:				
Home equity	8.2	5.7	8.8	6.8
Other	2.0	1.4	1.5	1.2
First mortgage	1.6	1.1	2.1	1.6
Asset-backed:				
Other	2.9	2.0	2.4	1.8
Auto	2.6	1.8	1.9	1.4
Leasing	2.1	1.5	2.4	1.9
Pooled corp. obligation and other	4.7	3.3	2.3	1.8
Financial risk	0.6	0.4	0.6	0.5
Total structured finance	24.7	17.2	22.0	17.0
Total domestic	116.0	80.9	107.7	83.5
International Infrastructure:				
Transportation	1.7	1.2	1.2	0.9
Sovereign	1.6	1.1	1.4	1.1
Utilities	1.1	0.8	0.7	0.5
Sub-sovereign	0.8	0.6	0.9	0.7
Investor owned utilities	0.6	0.4	0.5	0.4
Health care	0.4	0.3	0.4	0.3
Total infrastructure	6.2	4.4	5.1	3.9
Structured finance:				
Pooled corp. obligation and other	15.0	10.4	9.5	7.4
Financial risk	2.8	2.0	3.1	2.4
Asset-backed	1.8	1.2	2.4	1.9
Mortgage-backed	1.5	1.1	1.2	0.9
Total structured finance	21.1	14.7	16.2	12.6
Total international	27.3	19.1	21.3	16.5
Total	$143.3	100.0%	$129.0	100.0%

As part of MBIA Corp's reinsurance activity in 1998, MBIA Corp. entered into facultative reinsurance agreements with highly rated reinsurers that obligate it to cede future premiums to the reinsurers through January 1, 2005. Certain reinsurance contracts in 1998 were accounted for on a retroactive basis in accordance with SFAS 113, ''Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts''.

Components of premiums written including reinsurance assumed from and ceded to other companies is set forth in the following table:

	Years ended December 31,		
	2000	**1999**	**1998**
Direct	$641,452	$590,597	$664,269
Assumed	45,956	34,274	12,781
Gross	687,408	624,871	667,050
Ceded	(189,316)	(171,256)	(156,064)
Net	$498,092	$453,615	$520,986

Ceding commissions received from reinsurers before deferrals were $37.3 million, $35.3 million and $37.2 million in 2000, 1999 and 1998, respectively.

13. Employee Benefits

MBIA Corp. participates in MBIA Inc.'s pension plan covering substantially all employees. The pension plan is a defined contribution plan and MBIA Corp. contributes 10% of each eligible employee's annual total compensation. Pension expense for the years ended December 31, 2000, 1999 and 1998 was $4.9 million, $6.7 million and $5.9 million, respectively. MBIA Corp. also has a profit-sharing/401(k) plan which allows eligible employees to contribute up to 10% of eligible compensation. MBIA Corp. matches employee contributions up to the first 5% of eligible compensation. MBIA Corp. contributions to the profit-sharing/401(k) plan aggregated $1.9 million, $3.2.million and $2.6 million for the years ended December 31, 2000, 1999 and 1998, respectively. The profit-sharing/401(k) plan match amounts are invested in common stock of MBIA Inc. Amounts relating to the above plans that exceed limitations established by federal regulations are contributed to a non-qualified deferred compensation plan. In 2000, 1999 and 1998, former CMAC employees were covered under MBIA Inc.'s pension and profit-sharing/401(k) plans.

MBIA Corp. also participates in the ''MBIA Long-Term Incentive Program''. The incentive program includes a stock option program and adds a compensation component linked to the growth in adjusted book value per share (ABV) of MBIA Inc.'s stock. Awards under the long-term program are divided equally between the two components, with 50% of the award given in stock options and 50% of the award paid in cash or shares of MBIA Inc.'s stock.

Target levels for the option/incentive award are established as a percentage of total salary and bonus, based upon the recipient's position. Awards under the long-term program typically will be granted from the vice president level up to and including the chairman and chief executive officer.

The ABV portion of the long-term incentive program may be awarded every year. The 2000 award covers growth in ABV from December 31, 2000 through December 31, 2003; with a base line growth of 13.5%. The 1999 award covers growth in ABV from December 31, 1999 through December 31, 2002 and the 1998 award covers growth in ABV from December 31, 1998 through December 31, 2001, with a base line growth of 12% on both awards. The amount to be paid in respect of such award will be adjusted upward or downward based on the actual ABV growth with a minimum growth of 8% necessary to receive any payment and an 18% growth needed to receive the maximum payment of 200% of the target levels. The amount, if any, to be paid under this portion of the program will be paid in early 2004 for the 2000 award, in early 2003 for the 1999 award and in early 2002 for the 1998 award in the form of cash or shares of MBIA Inc.'s common stock. Subsequent awards, if any, will be made every year with concomitant payments occurring after the three-year cycle. During 2000, 1999 and 1998, $11.6 million, $7.2 million and $4.8 million, respectively, were recorded as compensation expense related to ABV awards.

MBIA Corp. also participates in MBIA Inc.'s restricted stock program, adopted in December 1995, whereby key executive officers of MBIA Corp. are granted restricted shares of MBIA Inc. common stock. These stock awards may only be sold three to five years from the date of grant, at which time the awards fully vest. Compensation expense related to the restricted stock was $2.2 million, $1.7 million and $0.9 million for the years ended December 31, 2000, 1999 and 1998.

In October 1995, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards (SFAS) 123, ''Accounting for Stock-Based Compensation,'' effective for financial statements for fiscal years beginning after December 15, 1995. SFAS 123 required MBIA Inc. to adopt, at its election, either 1) the provisions in SFAS 123 which require the recognition of compensation expense for employee stock-based compensation plans, or 2) the provisions in SFAS 123 which require the pro-forma disclosure of net income and earnings per share as if the recognition provisions of SFAS 123 had been adopted. MBIA Inc. adopted the disclosure requirements of SFAS 123 effective January 1, 1996 and continues to account for its employee stock-based compensation plans under Accounting Principles Board Opinion No. 25, ''Accounting for Stock Issued to Employees'' Accordingly, the adoption of SFAS 123 had no impact on MBIA Corp.'s financial position or results of operations. Had compensation cost for the MBIA Inc. stock option program been recognized based on the fair value at the grant date consistent with the recognition provisions of SFAS 123, the impact on MBIA Corp.'s net income would not have been material.

14. Related Party Transactions

Since 1989, MBIA Corp. has executed five surety bonds to guarantee the payment obligations of the members of the Association who had their Standard & Poor's Corporation claims-paying rating downgraded from Triple-A on their previously issued Association policies. In the event that they do not meet their Association policy payment obligations, MBIA Corp. will pay the required amounts directly to the paying agent. The aggregate outstanding exposure on these surety bonds as of December 31, 2000 is $340 million.

Included in other assets at December 31, 2000 and 1999 were $48.6 million and $64.2 million net receivables from MBIA Inc. and other subsidiaries.

MBIA Corp. entered into an agreement with MBIA Inc. and IMC whereby MBIA Corp. held securities subject to agreements to resell of $330 million and $205.0 million as of December 31, 2000 and 1999, respectively, and transferred securities subject to agreements to repurchase of $330 million and $205.0 million as of December 31, 2000 and 1999. These agreements have a term of less than one year. The interest expense relating to these agreements was $17.4 million and $10.9 million, respectively, for the years ended December 31, 2000 and 1999. The interest income relating to these agreements was $18.0 million and $11.5 million, respectively, for the years ended December 31, 2000 and 1999.

15. Fair Value of Financial Instruments

The estimated fair value amounts of financial instruments shown in the following table have been determined by MBIA Corp. using available market information and appropriate valuation methodologies. However, in certain cases considerable judgment is necessarily required to interpret market data to develop estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amount MBIA Corp. could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

Fixed-maturity securities – The fair value of fixed-maturity securities is based upon quoted market price, if available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Short-term investments – Short-term investments are carried at amortized cost which approximates fair value.

Other investments – Other investments include MBIA Corp.'s interest in equity oriented investments. The fair value of these investments is based on quoted market prices.

Cash and cash equivalents, receivable for investments sold and payable for investments purchased – The carrying amounts of these items are a reasonable estimate of their fair value.

Securities purchased under agreements to resell – The fair value is estimated based upon the quoted market prices of the transactions' underlying collateral.

Prepaid reinsurance premiums – The fair value of MBIA Corp.'s prepaid reinsurance premiums is based on the estimated cost of entering into an assumption of the entire portfolio with third party reinsurers under current market conditions.

Deferred premium revenue – The fair value of MBIA Corp.'s deferred premium revenue is based on the estimated cost of entering into a cession of the entire portfolio with third party reinsurers under current market conditions.

Loss and loss adjustment expense reserves – The carrying amount is composed of the present value of the expected cash flows for specifically identified claims combined with an estimate for unallocated claims. Therefore, the carrying amount is a reasonable estimate of the fair value of the reserve.

Securities sold under agreements to repurchase – The fair value is estimated based upon the quoted market prices of the transactions' underlying collateral.

Installment premiums – The fair value is derived by calculating the present value of the estimated future cash flow stream discounted at 9%.

Derivatives – The fair value reflects the estimated amounts that the MBIA Corp. would receive or pay to terminate the transaction at the reporting date.

	As of December 31, 2000		As of December 31, 1999	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
	(In thousands)			
ASSETS:				
Fixed-maturity securities	6,665,533	6,665,533	$5,783,979	$5,783,979
Short-term investments	269,900	269,900	273,816	273,816
Other investments	9,663	9,663	8,425	8,425
Cash and cash equivalents	12,541	12,541	33,702	33,702
Securities purchased under agreements to resell	330,000	396,951	205,000	267,881
Prepaid reinsurance premiums	442,622	380,047	403,210	342,837
Reinsurance recoverable on unpaid losses	31,414	31,414	30,819	30,819
Receivable for investments sold	2,497	2,497	2,882	2,882
LIABILITIES:				
Deferred premium revenue	2,397,578	2,123,661	2,310,758	2,022,357
Loss and loss adjustment expense reserves	499,279	499,279	467,279	467,279
Securities sold under agreements to repurchase	330,000	390,367	205,000	209,894
Payable for investments purchased	2,334	2,334	18,948	18,948
Off-balance sheet instruments:				
Installment premiums	—	885,477	—	731,748
Derivatives*	—	16,454	—	—

* The estimated fair value for 2000 includes net derivative liabilities identified as part of the company's implementation of SFAS 133.

MBIA ASSURANCE S.A.

AUDITOR'S REPORT ON THE FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2000

AUDITOR'S REPORT ON THE FINANCIAL STATEMENTS
Year ended December 31, 2000

To the Shareholders of MBIA Assurance S.A.
112, avenue Kléber
75116 Paris

In accordance with the terms of our appointment at the Annual Shareholders' Meeting, we hereby submit our report for the year ended December 31, 2000, on:

— our examination of the financial statements of MBIA Assurance, presented in French francs, as attached to this report,

— the specific procedures and information required by law.

These financial statements are the responsibility of the Board of Directors. Our responsibility is to express an opinion on these financial statements based on our audit.

I. Opinion on the financial statements

We conducted our audit in accordance with the professional standards applied in France. Those standards require that we plan and perform our audit to obtain reasonable assurance that the financial statements are free from material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made in the preparation of the financial statements, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements present fairly, in all material respects the assets and liabilities and financial position of the Company at December 31, 2000 and the results of operations for the year then ended in accordance with French generally accepted accounting principles.

Without qualifying the above opinion, we draw the shareholders' attention to note (Ic) which describes the change made in the determination of the reserves for unearned premiums and the corresponding impact to the financial statements for the year ended December 31, 2000.

II. Specific procedures and information

We have also performed the specific procedures required by law, in accordance with professional standards applied in France.

We are satisfied that the information given in the report of the Board of Directors and the documents sent to shareholders on the financial position and financial statements is fairly stated and agrees with those financial statements.

We have also verified that details of controlling and other interests acquired during the year and the identity of shareholders are disclosed in the report of the Board of Directors.

April 17, 2001

Statutory Auditor
Coopers & Lybrand Audit
Member of PricewaterhouseCoopers

Catherine Thuret

MBIA ASSURANCE S.A.

FINANCIAL STATEMENTS: BALANCE SHEETS AND PROFIT AND LOSS ACCOUNTS

	At December 31, 2000	At December 31, 1999
	(in French francs)	
ASSETS		
Investment		
Other investments	409,997,729	346,516,179
	409,997,729	**346,516,179**
Reinsurer's share in technical reserves		
Unearned premiums and premium deficiency reserves		
Related parties	4,756,114	9,330,963
Third party reinsurers	161,886,085	101,696,906
	166,462,199	**111,027,869**
Debtors		
Amounts receivable from Parent company	35,187,733	36,546,966
Other insurance debtors	500,058	1,128,779
Other reinsurance debtors	1,086,430	—
Prepaid and recoverable taxes	4,353,717	7,665
Sundry debtors		
Related parties	3,807,608	2,734,433
Other	12,823	21,690
Titrimmo guarantee deposit	25,498,864	39,506,253
	70,447,233	**79,945,786**
Other assets		
Tangible assets	2,741,731	812,351
Other deposits and guarantees	263,826	200,854
Cash and cash equivalents	23,776,900	4,420,472
	26,782,457	**5,433,677**
Prepayments and accrued income		
Other	1,568,738	219,932
Accrued interest and rental income	3,327,675	1,581,098
	4,896,413	**1,801,030**
Unrealised exchange losses	**24,466,147**	**14,813,301**
TOTAL ASSETS	**703,232,178**	**559,537,842**

MBIA ASSURANCE S.A.

FINANCIAL STATEMENTS: BALANCE SHEETS AND PROFIT AND LOSS ACCOUNTS

	At December 31, 2000	At December 31, 1999
	(in French francs)	
LIABILITIES		
Shareholders' equity		
Share capital	175,000,000	175,000,000
Legal reserve	30,196	30,196
Retained earnings/(deficit)	38,241,031	23,391,808
Net income/(loss) for the year	(1,021,403)	14,849,224
	212,249,824	**213,271,228**
Gross technical reserves		
Unearned premiums reserves and outstanding risks	348,771,443	238,707,532
	348,771,443	**238,707,532**
Provisions for liabilities and charges		
Provision for exchange losses	16,196,445	11,655,016
	16,196,445	**11,655,016**
Cash deposits received from reinsurer	**14,400,000**	**14,400,000**
Other liabilities		
Amounts due to parent company	20,881,505	—
Reinsurance creditors		
Related parties	13,051,817	12,582,162
Third party reinsurers	31,397,027	15,999,987
Other liabilities		
Other cash deposits received	7,545,800	7,545,800
Other loans	116,801	—
Accrued personnel costs	283,519	241,511
Accrued taxes and social security charges	1,281,319	495,932
Sundry creditors	1,189,768	396,690
Titrimmo	25,498,864	39,506,253
	101,246,420	**76,768,335**
Accruals and deferred income		
Other accruals	2,098,343	1,577,446
	2,098,343	**1,577,446**
Unrealised exchange gains	**8,269,703**	**3,158,285**
TOTAL LIABILITIES	**703,232,178**	**559,537,842**

MBIA ASSURANCE S.A.

FINANCIAL STATEMENTS: BALANCE SHEETS AND PROFIT AND LOSS ACCOUNTS

	2000 Gross	Ceded business	2000 Net	1999 Net
		(In French francs)		
NON LIFE INSURANCE TECHNICAL ACCOUNT				
Earned premiums				
Premiums	130,005,953	(70,776,904)	59,229,049	35,837,490
Change in unearned premiums reserve *(see note Ic)*	(104,856,663)	50,563,109	(54,293,554)	(16,549,901)
Allocated investment income	16,397,992		16,397,992	5,063,727
Other technical income	2,662,659		2,662,659	384,975
Acquisition and administration costs				
Acquisition costs	(17,830,930)		(17,830,930)	(2,095,395)
Administration costs	(19,168,482)		(19,168,482)	(2,828,565)
Reinsurance commissions received		1,950,871	1,950,871	2,313,832
Non-life underwriting result	**7,210,529**	**(18,262,924)**	**(11,052,395)**	**22,126,163**
NON-TECHNICAL ACCOUNT OF NON-LIFE INSURANCE				
Investment income				
Investment revenues			5,339,761	5,315,007
Other investment income			19,363,160	15,002,519
Gains on disposal of investments			33,136,803	5,967,093
Investment expense				
Interest and portfolio expenses			(221,457)	(1,507,571)
Other investment expenses			(374,942)	(467,113)
Losses on disposal of investments			(22,285,633)	(12,760,527)
Investment income transferred to the technical accounts			(16,397,992)	(5,063,727)
Other non-underwriting income			7,188	46,371
Other non-underwriting expense			(47,769)	(9,783)
Non-recurring income/expense				
Non-recurring income				
Non-recurring expense				(23,591)
Income tax			(8,488,127	(13,775,619
Non-technical result on non-life insurance			**10,030,992**	**(7,276,941)**
INCOME FOR THE YEAR			**(1,021,403)**	**14,849,224**

NOTES TO THE FINANCIAL STATEMENTS

I. ACCOUNTING POLICIES AND METHODS

The financial statements for the years ended December 31, 2000 and 1999 have been prepared in accordance with the provisions of the revised French Insurance Code. The company does not own any subsidiaries and therefore does not produce consolidated accounts. During the year 2000, the company has established a branch in the United Kingdom which accounts are included in the financial statements of MBIA SA for the year ended December 31, 2000.

Significant accounting principles which are summarised below remain unchanged compared to 1999, with the exception of the change in the calculation of the reserves of unearned premiums as explained in note (c).

(a) Investments

Bonds and other fixed income securities are stated at cost, excluding interest accrued at the date of acquisition. Premiums and discounts on bonds and other fixed income securities (difference between the purchase price and the redemption price) are written off to the profit and loss account over the residual lives of the securities, in accordance with the article R.332-19 of the French Insurance Code.

The accumulated amortisation is recorded under ''accruals and other assets'' or ''accrual and other liabilities''.

At year-end, no provision is made for unrealised losses corresponding to the difference between the amortised cost of securities and their fair market value. However a provision for counter party risks is recorded if the company has reason to believe that the issuer will be unable to fulfil its obligations in terms of the payment of interests or principle repayments (Article R.332-19).

Equities and other variable income securities are stated at cost, excluding accrued interest at the acquisition date. Disposals are determined by the First In-First Out method (FIFO).

At year-end, the realisable value corresponds to market value, determined by the method prescribed by the French Insurance Code. A provision is recorded, separately for each line of securities, only if the diminution in value is qualified as permanent.

In addition, a liquidity risks reserve is set up if the total carrying value of investments (excluding securities carried at amortised cost) exceeds the total net book value of all assets concerned. The liquidity risks reserve is shown in the balance sheet under ''other technical reserves''.

(b) Exchange gains and losses

Foreign currency transactions are translated into French francs at the year-end exchange rate.

Exchange gains for all currencies combined are included in liabilities. Exchange losses are included in assets. A related provision is recorded in case of net exchange loss.

(c) Technical reserves

For the year ended December 31, 2000, the company has changed the method used to determine reserves for unearned premiums.

The method used until December 31, 1999, which was previously approved by the *Commission de Contrôle des Assurances*, complied with the provisions of the French Insurance Code (Article A.331-16) stating, ''reserves for unearned premiums are to be calculated on an accrual basis''.

For the year ended December 31, 2000, the *Commission de Contrôle des Assurances* has amended their position on how the Company determines reserves for unearned premiums. In order to better comply with prudential principles as described in article R.333-1 of the French Insurance Code to determine the unearned premium reserves and with the provisions of Article 57-2 of the European Directive n°91/674/CEE of December 19, 1991 which states that: ''In classes of insurance where the assumption of a temporal correlation between risk experience and premium is not appropriate, calculation methods shall be applied that take account of the differing pattern of risk over time'', the *Commission de Contrôle des Assurances* requested that the amount of unearned premium reserves be determined based on the maturities of the insured debt issues, rather than on a straight line basis over the life of the issues.

As such, the implementation of the method required by the *Commission de Contrôle des Assurances* amounts to applying in advance European provisions that have not yet been transposed into the French Insurance Code.

The *Commission de Contrôle des Assurances* also required that the new calculation be applied retrospectively to include premiums written prior to January 1, 2000. Adjusting the unearned premium reserve as of January 1, 2000 to reflect this change, amounts to a charge of 25 116 329 FF (reversal of earned premiums), in the profit and loss account for the year ended December 31, 2000.

Premiums reversed as a result of this change will be recorded as income in the profit and loss account under the new method described above.

(d) Expense allocation

Effective from January 1, 1995, a distinction is made between acquisition and administration costs. These costs mainly correspond to personnel expenses which are allocated based on the position occupied by each employee.

Acquisition costs are not deferred because they consist primarily of fixed costs.

A percentage of net investment income is transferred from the non-technical account to the technical account on the basis of the shareholder's equity/shareholders' equity + net technical reserve ratio.

(e) Tangible fixed assets used in the business

Tangible fixed assets are stated at cost. Maintenance charges are charged to the profit and loss account when incurred, except where they serve to increase productivity or extend the useful life of the asset concerned.

Depreciation is calculated by the straight-line method over the estimated useful life of the assets, in accordance with French tax rules. The main estimated useful lives are as follows:

Leasehold improvements, fixtures and fittings	8 years
Vehicles	5 years
Office and computer equipment	4 years
Furniture	5 to 8 years

II. NOTES TO THE BALANCE SHEET

(a) Investment portfolio

Investments recorded in the balance sheet at December 31, 2000 in accordance with Article R.332 -20 of the French Insurance Code are as follows:

Description of securities	Number	At cost	Unit market price	Market value	Realised/ (unrealised gains)
Long-term investments					
OAT		27,404,147.03		27,404,147.03	
BTAN		158,907,864.69		158,907,864.69	
Total		**186,312,011.72**		**186,312,011.72**	
Short term investments					
Credis EUR	874	1,970,864.79	2,353.18	2,056,679.44	85,814.66
Credis GBP	2,990	103,780,118.80	35,887.61	107,303,942.29	3,523,823.49
Credis USD	1,130	19,154,946.84	17,526.00	19,804,380.93	649,434.09
Credis CAD	317	2,210,855.15	8,211.51	2,603,048.89	392,163.74
PIM	3	3,342,992.10	1,169,296.94	3,507,890.83	164,898.73
FCP Berri Monet	11	1,679,530.15	156,169.91	1,717,869.06	38,338.91
FCP Primerus monet	1,059	15,993,399.66	15,532.47	16,448,887.21	455,487.55
FCP Fructifonds	411	74,197,286.25	181,125.35	74,442,518.84	245,232.59
Compte à terme HKD		1,355,693.87		1,355,693.87	
Total		**223,685,717.60**		**229,240,911.36**	**5,555,193.77**
TOTAL		**409,997,729.32**		**415,552,923.09**	**5,555,193.77**

All the above investments have been valued in accordance with Article R 332-20 of the French Insurance Code. The realisable value of the securities corresponds to their market value at December 31, 2000.

(b) Debtors and creditors

At December 31, 2000 all debtors and creditors were due within one year, with the exception of those relating to the Titrimmo operation (securitisation of property receivables) for an amount of FRF 25,498,864.

(c) Related party debtors and creditors

Debtors	Reinsurers' share of technical reserves	Insurance debtors	Current account
MBIA Insurance Corporation and branches	4,756,114	0	35,187,733

Creditors	Reinsurance creditors	Guarantee deposit	Current account
MBIA	13,051,817	14,400,000	20,881,505

(d) Share capital and changes in shareholders' equity

At December 31, 2000, the Company's issued share capital was made up of 1,750,000 ordinary shares with a par value of FRF 100 each. MBIA Insurance Corporation held 99.99% of the capital at that date.

Changes in shareholders' equity during 2000 were as follows :

	At January 1, 2000	Appropriation of 1999 profit	2000 loss	At December 31, 2000
		(in FF thousands)		
Share capital	175,000			175,000
Legal reserve	30			30
(Deficit)/retained earnings	23,392	14,849		38,241
Profit/(loss)	14,849	(14,849)	(1,021)	(1,021)
Total	**213,271**	**0**	**(1,021)**	**212,250**

III. NOTES TO THE PROFIT AND LOSS ACCOUNT

(a) Investment income and expenses

	Other investment revenues and expenses
Revenues from investments in subsidiaries and affiliates	—
Revenues from property holdings	—
Other investment revenues	5,339,761
Total	**5,339,761**
Investment expenses	—

Breakdown of other investment income

	(in FF thousands)
Exchange gain on investments	7,662
Amortization of capital gains	46
Reversal of provision for exchange loss on investments	11,655
Total	**19,363**

(b) Breakdown of investment expenses

	(in FF thousands)
Interest and bank fees	221
Amortization of capital losses	375
Charge to provision for exchange loss on investments	16,197
Exchange losses on investments	6,089
Total	**22,882**

(c) Additional notes to the profit and loss account

Personnel costs

Personnel costs for the period 1998 to 2000 break as follows:

	2000	1999	1998
Wages and salaries	2,296,301	855,000	1,038,868
Pension benefits	—	—	—
Social security taxes	832,830	401,981	440,309
Other	1,516,372*	15,499	(32,470)
Total	**4,645,503**	**1,272,480**	**1,446,707**

* of which, UK branch: 1,180,154 FF

Breakdown of gross premiums written

Gross premiums written in the period 1998 to 2000 can be analysed as follows:

	2000	1999	1998
		(By business in FF)	
Local authority credit enhancement	1,549,850	11,862,135	2,746,373
Structured financing	14,671,684	15,344,410	19,737,771
Concessions and corporations	113,784,419	65,574,934	—
Total	**130,005,953**	**92,781,479**	**22,484,144**

	2000	1999	1998
		(By geographic region in FF)	
Europe	129,391,144	91,873,474	21,186,333
France	*4,073,191*	*16,261,909*	*9,678,344*
The Americas	—	66,716	301,742
Asia	614,809	841,289	996,069
Total	**130,005,953**	**92,781,479**	**22,484,144**

IV. OTHER INFORMATION

(a) Consolidating entity

MBIA Assurance S.A. is a 99.99% owned subsidiary of MBIA Insurance Corporation which has its principal place of business at 113 King Street, Armonk, NewYork, 10504 U.S.A.

(b) Average number of employees

The average number of employees of the Company totalled 2 persons in 2000 and 1999. In addition MBIA Insurance Corporation provides secondments to the UK branch of MBIA Assurance SA.

(c) Off-balance sheet commitments

At December 31, 2000, the Company had received reinsurance commitments (pledged securities and cash deposits) from the reinsurer AMBAC Assurance Corporation, amounting to 65,268,592 FF as follows:

— cash deposit of 2,616,642 GBP (27,502,073 FF)

— cash deposit of 1,358 EUR (8,911 FF)

— 234 Berri Monétaire C of 23,807,95 EUR each (36,543,760 FF)

— 42 Berri Trésor C of 4,405,95 EUR each (1,213,848 FF)

At December 31, 2000, the Company had no other material off-balance sheet commitments and did not carry out any financial instruments transactions.

Appendix D

AUDITED ACCOUNTS OF DCC

FINANCIAL INFORMATION RELATING TO DWR CYMRU CYFYNGEDIG

Basis of information

The information set out on pages D2 to D21 includes financial information for the two financial years ended 31 March 2000, which is extracted, without material adjustment, from the audited financial statements for each of the two years. The financial statements have been prepared under UK generally accepted accounting standards.

The information set out on pages D2 to D21 does not constitute full statutory accounts within the meaning of section 240(5) of the Companies Act. The reports of the auditors, PricewaterhouseCoopers, on the accounts for the two years ended 31 March 2000 were unqualified and contained no statements as are referred to in section 237(2) or (3) of the Companies Act. Statutory accounts for the two financial years ended 31 March 2000 have been delivered to the Registrar of Companies in England and Wales.

PRINCIPAL ACCOUNTING POLICIES

The financial statements have been prepared in accordance with Accounting Standards applicable in the United Kingdom and, except for the treatment of certain grants and contributions, comply with the Companies Act 1985. An explanation of this departure from the requirements of the Companies Act 1985 is given in the ''Grants and customer contributions'' section below and note 9(c). A summary of the principal accounting policies, which have been consistently applied, is shown below.

Changes in presentation of financial information

Since the previous directors' report and financial statements, the Accounting Standards Board has issued Financial Reporting Standard 16- Current Tax. In addition the Urgent Issues Task Force (''**UITF**'') has issued a number of abstracts in the year. Where relevant, these financial statements comply with the new standards and UITF abstracts and have adopted in full FRS 15-Tangible Fixed Assets.

Basis of accounting

These financial statements have been prepared in accordance with the historical cost convention.

Turnover

Turnover represents the income receivable in the ordinary course of business for services provided and excludes value added tax.

Exceptional items

Exceptional items are those that need to be disclosed by virtue of their size and incidence. Such items are included within operating profit unless they represent profits or losses on the sale or termination of an operation, costs of a fundamental reorganisation or restructuring having a material effect on the nature and focus of the company, or profits or losses on the disposal of fixed assets. In these cases, separate disclosure is provided on the face of the profit and loss account after operating profit.

Tangible fixed assets and depreciation

Tangible fixed assets comprise:

(i) infrastructure assets (being mains and sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls); and

(ii) other assets (including properties, overground operational structures and equipment and fixtures and fittings).

Infrastructure assets

Infrastructure assets comprise a network of systems. Expenditure on infrastructure assets relating to increases in capacity, enhancements or replacements of the network is treated as additions which are included at cost after deducting grants and contributions.

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 the company's independently certified asset management plan.

Other assets

Other assets are included at cost less accumulated depreciation. Freehold land is not depreciated. Other assets are depreciated over their estimated useful economic lives, which are principally as follows:

Freehold buildings	30-60 years
Leasehold properties	over the period of the lease
Operational structures	40-80 years
Fixed plant	20-40 years
Vehicles, mobile plant, equipment and computer hardware & software	3-16 years

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

Leased assets

Where assets are financed by leasing arrangements which transfer substantially all the risks and rewards of ownership of an asset to the lessee (finance leases), the assets are treated as if they had been purchased and the corresponding capital cost is shown as an obligation to the lessor. Leasing payments are treated as consisting of a capital element and finance costs, the capital element reducing the obligation to the lessor and the finance charges being written off to the profit and loss account over the period of the lease in reducing amounts in relation to the written down amount. The assets are depreciated over the shorter of their estimated useful life and the lease period. All other leases are regarded as operating leases. Rental costs arising under operating leases are charged to the profit and loss account in the year to which they relate.

Grants and customer contributions

Grants and customer contributions relating to infrastructure assets have been offset against fixed assets (see note 9(c)).

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

Investments

Long term investments held as fixed assets are stated at cost less amounts written off or provided to reflect permanent diminution in value. Those held as current assets are stated at the lower of cost and net realisable value.

Stocks and work in progress

Stocks are stated at the lower of cost and net realisable value which takes account of any provision necessary to recognise damage and obsolescence. Work in progress is valued at the lower of cost and net realisable value. Cost includes labour, materials, transport and directly attributable overheads.

Pension costs

Contributions are charged to the profit and loss account so as to spread the cost of pensions over employees' working lives with the company. Contribution rates are based on the advice of a professionally qualified actuary. Any difference between the charge to the profit and loss account and contributions paid is shown as an asset or liability in the balance sheet.

Interest rate swaps

Interest differentials, under swap arrangements used to manage interest rate exposure on borrowings and current asset investments, are recognised by adjusting interest payable or receivable as appropriate.

Research and development

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

Deferred taxation

Provision is made for deferred taxation, using the liability method, on all material timing differences to the extent that it is probable that a liability or asset will crystallise.

Profit and Loss Account for the Year Ended 31 March 2000

	Note	2000 £m	1999 £m
Turnover	2	476.9	459.3
Net operating costs	3	(324.9)	(292.9)
Operating profit		152.0	166.4
Before exceptional items:			
Continuing operations		186.1	166.4
Exceptional items	4	(34.1)	—
Operating profit		152.0	166.4
Profit on disposal of fixed assets		0.3	0.5
Profit on ordinary activities before interest		152.3	166.9
Interest receivable		2.7	6.1
Interest payable	6	(57.0)	(58.0)
Profit on ordinary activities before taxation		98.0	115.0
Taxation	7	1.1	(8.9)
Profit on ordinary activities after taxation		99.1	106.1
Dividends on preference shares	8	(14.0)	(14.0)
Profit attributable to ordinary shareholder		85.1	92.1
Dividends on ordinary shares	8	(15.0)	(44.0)
Retained profit for the year	22	70.1	48.1

All operations are continuing.

The company has no recognised gains and losses other than the profits above and therefore no separate statement of total recognised gains and losses has been presented.

There is no difference between the results disclosed above and the results on an unmodified historical cost basis.

Balance Sheet at 31 March 2000

	Note	2000 £m	1999 £m
Fixed assets			
Tangible assets	9	2,144.3	1,980.6
Investments	10	0.1	0.1
		2,144.4	1,980.7
Current assets			
Stocks and work in progress	11	3.8	6.0
Debtors	12	88.9	101.9
Current asset investments	13(a)	37.8	71.9
Cash at bank and in hand		7.3	1.6
		137.8	181.4
Current liabilities			
Creditors: amounts falling due within one year	14(a)	(309.8)	(244.0)
Net current (liabilities)		(172.0)	(62.6)
Total assets less current liabilities		1,972.4	1,918.1
Creditors: amounts falling due after more than one year	14(b)	(781.9)	(792.8)
Provisions for liabilities and charges	19	(16.1)	(21.0)
Deferred income	20	(40.3)	(40.3)
Net assets		1,134.1	1,064.0
Capital and reserves			
Called up share capital	21	476.1	476.1
Reserves	22	658.0	587.9
Equity shareholders' funds		934.1	864.0
Non-equity shareholders' funds		200.0	200.0
Total shareholders' funds		1,134.1	1,064.0

The financial statements on pages D1 to D21 were approved by the Board of directors on 11 July 2000 and were signed on its behalf by:

M Brooker
Managing Director

G J Miles
Finance Director

Cashflow Statement for the Year Ended 31 March 2000

	Note	2000 £m	1999 £m
Cash flow from operating activities	23	253.3	248.0
Returns on investments and servicing of finance			
Interest received		2.8	7.9
Interest paid		(44.9)	(43.8)
Preference dividends paid		(14.0)	(21.0)
Interest element of finance lease rental payments		(16.2)	(9.7)
		(72.3)	(66.6)
Taxation			
UK corporation tax paid		(11.2)	(5.5)
Group relief received/(paid)		3.6	(9.1)
		(7.6)	(14.6)
Capital expenditure and financial investment			
Purchase of tangible fixed assets		(242.1)	(287.7)
Sale of tangible fixed assets		0.8	0.8
Grants and contributions received		7.0	11.1
		(234.3)	(275.8)
Equity dividends paid		(34.7)	(28.0)
Cash outflow before use of liquid resources and financing		(95.6)	(137.0)
Management of liquid resources Net decrease in deposits		34.1	61.1
Financing			
Loan received from parent undertaking		100.0	40.0
Loan repaid to parent undertaking		—	(40.0)
Loan repayments		(36.3)	(7.0)
Finance lease received		—	92.1
		63.7	85.1
Increase in cash in the year	24	2.2	9.2

Reconciliation of Movements in Shareholder's Funds for the Year Ended 31 March 2000

	2000 £m	1999 £m
Profit for the year attributable to ordinary shareholder	85.1	92.1
Ordinary dividends	(15.0)	(44.0)
Net increase in shareholders' funds	70.1	48.1
At 1 April	1,064.0	1,015.9
At 31 March	1,134.1	1,064.0

Notes to the Financial Statements

1. Consolidated financial statements

The company has taken advantage of Section 228(1) of the Companies Act 1985 not to produce consolidated financial statements as it is a wholly owned subsidiary of Hyder plc.

2. Segmental analysis by class of business

(a) Turnover

	2000 £m	1999 £m
Regulated water and sewerage activities	472.7	456.0
Non regulated activities	4.2	3.3
	476.9	459.3

Turnover is stated net of customer rebates of £11.6m (1999 – £11.5m).

(b) Profit on ordinary activities before taxation

	2000 £m	1999 £m
Regulated water and sewerage activities		
Operating Profit*	151.6	166.1
Profit on disposal of fixed assets	0.3	0.5
Interest payable	(55.2)	(52.9)
	96.7	113.7

	2000 £m	1999 £m
Non-regulated activities		
Operating profit	0.4	0.3
Interest receivable	0.9	1.0
	1.3	1.3

* Operating results as disclosed above, are after deducting exceptional items of £34.1m (1999 - Nil) (see Note 4). The operating profit, prior to deducting the exceptional items, is set out below:

	2000 £m	1999 £m
Operating Profit	185.7	166.1

(c) Net Assets

	2000 £m	1999 £m
Regulated water and sewerage activities	1,116.5	1,047.7
Non-regulated activities	17.6	16.3
	1,134.1	1,064.0

All turnover and profit before taxation, by origin and destination, was attributable to the UK.

3. Net operating costs

	Note	2000 Before Except-ional Items £m	2000 Except-ional items (Note 4) £m	2000 Total £m	1999 Total £m
Staff costs	5(b)	47.6	—	47.6	51.1
Severance and redundancy costs	4	—	14.1	14.1	—
Depreciation:					
Own assets		70.3	—	70.3	67.1
Assets held under finance leases		10.4	—	10.4	9.4
Research and development		0.3	—	0.3	0.1
Rentals under operating leases:					
Hire of plant and equipment		8.1	—	8.1	7.8
Other		0.2	—	0.2	0.2
Fees paid to auditors:					
Audit services		0.1	—	0.1	0.1
Other services		0.1	—	0.1	0.1
Other operating charges		170.2	20.0	190.2	172.5
Amortisation of grants and contributions	20	(1.3)	—	(1.3)	(1.3)
Own work capitalised		(15.1)	—	(15.1)	(13.5)
Net rents receivable		(0.1)	—	(0.1)	(0.7)
		290.8	34.1	324.9	292.9

4. Exceptional items

	2000 £m
By type of provision	
Severance and redundancy costs	14.1
Bad debt provision	20.0
	34.1

During the financial year, the regulated utility and related managed services businesses of the Hyder group (including Dŵr Cymru Cyfyngedig) undertook a programme of reorganisation which involved job reductions. An element of the job reductions was within Dŵr Cymru Cyfyngedig. All job reductions were achieved by means of voluntary redundancy. To meet the cost of this restructuring a charge of £14.1m has been made for the year ended 31 March 2000. The effect of this exceptional item on the taxation charge for the period is £1.6m.

The company's ability to collect revenue from certain of its customers has been reduced due to the government's decision to ban water disconnections and its ruling on Watercard last year. Therefore the bad debt provision has been re-assessed and an exceptional charge of £20m has been made for the year. The effect of this exceptional item on the taxation charge for the period is £6.0m.

5. Directors and employees

(a) Directors' emoluments

The combined emoluments of the directors of Dŵr Cymru Cyfyngedig for their services as directors of the company is set out below:

	2000 £,000	1999 £,000
Aggregate emoluments and other benefits	578	527
Highest paid director: Aggregate emoluments and other benefits	134	94
Accrued pension under defined benefit scheme	42	77

Retirement benefits are accruing to eight directors (1999 – seven) under defined benefit schemes. No director has exercised share options in the company's ultimate parent company, Hyder Plc, during the year.

(b) Staff costs

	2000 £m	1999 £m
Wages and salaries	41.5	44.1
Social security costs	3.3	3.5
Pension costs	2.8	3.5
	47.6	51.1

Of the above, £9.2m (1999 £8.3m) has been charged to capital.

(c) Average monthly number of employees during the year (including executive directors)

	2000 Number	1999 Number
Regulated water and sewerage activities	1,737	1,906

6. Interest payable

	2000 £m	1999 £m
On bank loans and overdrafts	1.2	1.9
On other loans	43.7	42.6
On finance leases	12.1	13.5
	57.0	58.0

Included in other loans are amounts payable to group undertakings of £26.2m (1999 £24.6m).

7. Taxation

	2000 £m	1999 £m
Based on the results for the year:		
Group relief payable	8.3	17.3
	8.3	17.3
Prior year adjustments:		
Corporation tax receivable	(12.6)	(12.3)
Group relief payable	3.2	3.9
	(1.1)	8.9

The tax charge has been reduced by £20.9m (1999 £21.7m) in respect of excess tax allowances over depreciation and other timing differences, for which no provision is made.

The effect of an exceptional item on the taxation charge for the period is £7.6m as per note 4.

8. Dividends

	2000 £m	1999 £m
(a) Dividends on ordinary shares		
Interim paid: 1.81p per share (1999 5.19p per share)	5.0	14.3
Final proposed: 3.62p per share (1999 10.76p per share)	10.0	29.7
	15.0	44.0
(b) Dividends on preference shares		
Paid on 7% preference shares	14.0	14.0

9. Tangible fixed assets

(a) analysis by type

	Freehold land and buildings £m	Infra-structure assets £m	Operational structures £m	Vehicles, plant, equipment and computer hardware & software £m	Total £m
Cost					
At 1 April 1999	47.0	1,060.0	1,382.7	170.5	2,660.2
Additions	—	137.8	103.1	11.1	252.0
Grants and contributions	—	(6.6)		—	(6.6)
Disposals	(0.2)	(1.0)	—	—	(1.2)
Amounts written off in year	—	—	—	(0.3)	(0.3)
Transfers from Group Companies	1.6	—	—	—	1.6
At 31 March 2000	48.4	1,190.2	1,485.8	181.3	2,905.7
Accumulated depreciation					
At 1 April 1999	13.3	240.4	310.6	115.3	679.6
Charge for the year	0.6	34.7	36.6	8.8	80.7
Eliminated on disposal	(0.1)	(1.0)	—	—	(1.1)
Impairment losses	1.6				1.6
Transfers from Group Companies	0.6	—	—	—	0.6
At 31 March 2000	16.0	274.1	347.2	124.1	761.4
Net book value					
At 31 March 2000	32.4	916.1	1,138.6	57.2	2,144.3
At 31 March 1999	33.7	819.6	1,072.1	55.2	1,980.6
Analysis of net book value at 31 March 2000					
Owned	32.4	916.1	783.0	54.0	1,785.5
Held under finance leases	—	—	358.8	—	358.8
	32.4	916.1	1,141.8	54.0	2,144.3

Tangible fixed assets at 31 March 2000 include £358.0m (1999 £345.9m) of assets in the course of construction, which are not depreciated until commissioned.

9. Tangible fixed assets (continued)

(b) analysis by service

	Water Services £m	Sewerage Services £m	General £m	Total £m
Cost				
At 1 April 1999	1,151.6	1,348.4	160.2	2,660.2
Additions	60.3	183.8	7.9	252.0
Grants and contributions	(3.5)	(3.1)	—	(6.6)
Disposals	(0.6)	(0.4)	(0.2)	(1.2)
Assets written off in year	—	—	(0.3)	(0.3)
Transfers from Group Companies	—	—	1.6	1.6
At 31 March 2000	1,207.8	1,528.7	169.2	2,905.7
Accumulated Depreciation				
At 1 April 1999	274.1	305.4	100.1	679.6
Charge for the year	38.6	33.2	8.9	80.7
Eliminated on disposal	(0.6)	(0.4)	(0.1)	(1.1)
Impairment Losses	—	—	1.6	1.6
Transfers from Group Companies	—	—	0.6	0.6
At 31 March 2000	312.1	338.2	111.1	761.4
Net book value				
At 31 March 2000	895.7	1,190.5	58.1	2,144.3
At 31 March 1999	877.5	1,043.0	60.1	1,980.6
Analysis of net book value at 31 March 2000				
Owned	760.0	967.4	58.1	1,785.5
Held under finance leases	135.7	223.1	—	358.8
	895.7	1,190.5	58.1	2,144.3

(c) The accounting treatment for grants and customer contributions in respect of infrastructure assets is described in the principal accounting policies on D3. This treatment is not in accordance with Schedule 4 to the Companies Act 1985 which requires fixed assets to be shown at the purchase price or production cost and hence grants and contributions would be presented under the Act as deferred income. The treatment explained on D3 has been adopted in accordance with section 227(6) of the Companies Act 1985 in order to show a true and fair view, as in the opinion of the directors, it is not appropriate to treat grants and contributions on infrastructure assets as deferred income. The fixed assets to which they relate do not have determinable finite lives and any grants and contributions relating to such assets would not separately be taken to the profit and loss account, but are reflected in the depreciation charge. As a consequence the net book value for fixed assets and deferred income is £154.9m (1999 £148.3m) lower than it would have been had this treatment not been adopted.

10. Fixed asset investments

The company has £0.1m investments (1999 £0.1m) in the following entities all of whom are incorporated in Great Britain:

Subsidiary	Nature of Business	Description of Shares Held	Proportion Held
Welsh Water Utilities Finance PLC	Investment Company	£1 ordinary shares	100%
Joint Venture			
Hyder Utilities (Operations) Ltd	Operational Activities	£1 ordinary shares	50%

Equity of less than 10% in the following unlisted company:

Subsidiary	Nature of Business	Description of Shares Held	Proportion Held
Water Research Centre (1989) Plc	Water Research	Great Britain	"B" Ordinary Shares of £1

In addition, the Company holds 5% Convertible Unsecured Loan Stock 2014 at a cost of £23,326 in Water Research Centre (1989) Plc.

11. Stocks and work in progress

	2000 £m	1999 £m
Raw materials and consumables	3.3	5.0
Work in progress	0.5	1.0
	3.8	6.0

The replacement cost of stocks are not materially different from their carrying value.

12. Debtors

	2000 £m	1999 £m
Amounts falling due within one year:		
Trade debtors	35.6	40.2
Amounts owed by group undertakings	3.2	1.8
Other debtors	20.2	15.0
Prepayments and accrued income	29.8	37.3
	88.8	94.3
Amounts falling due after more than one year:		
Other debtors	0.1	7.6
	88.9	101.9

13. Current asset investments

(a) Management of liquid resources

	2000 £m	1999 £m
Investments in:		
Fixed term and call deposits	37.8	49.0
Other money market investments	—	22.9
	37.8	71.9
Amounts becoming due:		
Within one year	37.8	71.9
	37.8	71.9

Cash generated from operating activities and from long term loan drawdowns in advance of future capital expenditure obligations is invested on a daily basis by Hyder plc under an agency agreement in money market investments. These investments include term deposits, government securities and corporate bonds and papers rated at not less than AA.

(b) Interest rate swaps

The company has entered into interest rate swap arrangements in order to manage interest rate exposure of the company and not for trading or speculative purposes.

The company's interest rate swap arrangements, excluding the long dated interest rate swap specific to finance lease borrowing (note 16), had a notional principal balance of £ Nil (1999 £29.2m).

The arrangements terminated in December 1999. The interest rate at the date of termination was 6.12% (1999 6.12%).

14. Creditors

(a) Amounts falling due within one year

	Note	2000 £m	1999 £m
Bank loans and overdrafts		28.8	25.3
Other loans	15	8.1	36.3
Trade creditors		89.3	68.0
Amounts owed to group undertakings		110.8	16.0
Dividends payable		10.0	29.7
Corporation tax		—	0.4
Other taxation and social security		1.2	1.5
Other creditors		61.6	66.8
		309.8	244.0

Amounts owed to group undertakings include a loan of £100m at a variable interest rate payable at one month's notice.

(b) Amounts falling due after more than one Year

	Note	2000 £m	1999 £m
Loans	15	197.9	206.0
Obligations under finance leases	16	265.4	265.4
Amounts owed to group undertakings		317.3	317.3
Other creditors – between one and five years		1.3	4.1
		781.9	792.8

Amounts owed to group undertakings comprise loans of £99.1m and £98.2m at an interest rate of 7.55%, repayable in 2004 and 2014 respectively and loans of £60.0m and £60.0m at an interest rate of 7.84% repayable in 2007 and 2017 (1999 loans of £99.1m and £98.2m at interest rates of 7.55% repayable 2004 and 2014 and loans of £60.0m and £60.0m at an interest rate of 7.84% repayable in 2007 and 2017).

15. Other loans

	2000 £m	1999 £m
Repayable as follows:		
Within one year	8.1	36.3
Between one and two years	8.1	8.1
Between two and five years	24.2	24.2
After more than five years	165.6	173.7
	206.0	242.3
Repayable wholly within five years	—	29.2
Repayable wholly after five years	140.0	140.0
Repayable by instalments after five years	66.0	73.1
	206.0	242.3

Interest rates on these loans range between 4.98% and 10.15%. (1999 6.12% and 10.15%).

16. Finance leases

	2000 £m	1999 £m
Amounts due under finance leases after more than five years	265.4	265.4

A long dated interest rate swap was arranged on 1 April 1994 which has the effect of fixing the rate of interest at 7.8% on floating rate sterling finance lease obligations of £57.9m. This obligation reduces over a term of 14 years.

17. Capital commitments

	2000 £m	1999 £m
Contracted for but not provided in the financial statements	130.9	158.0

In order to meet additional quality and service standards, together with growth and new demands, the company has capital investment obligations over the next five years amounting to approximately £1.13 billion at current prices in the regulated water and sewerage business.

18. Leasing commitments

	Land and Buildings		Other	
	2000 £m	1999 £m	2000 £m	1999 £m
At 31 March 2000 there were revenue commitments, in the ordinary course of business in the next year for the payment of rentals on non cancellable operating leases expiring:				
Between two and five years	0.1	0.1	—	—
After five years	0.1	0.1	—	—
	0.2	0.2	—	—
Due to group undertaking expiring:				
Within one year	—	—	2.0	2.3
Between one and two years	—	—	1.3	1.6
Between two and five years	—	—	1.6	2.4
After five years	—	—	0.3	0.8
	—	—	5.2	7.1

19. Provisions for liabilities and charges

	Note	2000 £m	1999 £m
Deferred taxation	(a)	—	—
Restructuring provision	(b)	14.2	20.1
Provision for uninsured losses	(c)	1.9	0.9
		16.1	21.0

(a) Deferred taxation

No provision is required for deferred taxation in accordance with the policy described on D3. The amount unprovided of the total potential liability, is as follows:

	Amount provided		Amount unprovided	
	2000 £m	1999 £m	2000 £m	1999 £m
Tax effect of timing differences:				
Excess of tax allowances over depreciation	—	—	310.3	270.8
Other timing differences	—	—	(3.4)	(7.5)
	—	—	306.9	263.3

(b) Restructuring provision

This provision is in respect of payments to be made relating to the restructuring of the business for the items below and will be utilised over the next twelve months.

	Severance 2000 £m	**Property 2000 £m**	**Other 2000 £m**	**Total 2000 £m**
At 1 April	14.7	5.4	—	20.1
Charge to the profit and loss account	14.1	0.6	0.3	15.0
Utilised in the year	(16.4)	(4.5)	—	(20.9)
At 31 March	12.4	1.5	0.3	14.2

	Severance 1999 £m	**Property 1999 £m**	**Other 1999 £m**	**Total 1999 £m**
At 1 April	20.0	6.4	—	26.4
Utilised in the year	(5.3)	(1.0)	—	(6.3)
At 31 March	14.7	5.4	—	20.1

(c) Provision for uninsured losses

This provision is in respect of uninsured losses and its utilisation period is uncertain due to the nature of insurance claims.

	2000 £m	**1999 £m**
At 1 April	0.9	1.1
Charge for the year	1.5	0.3
Utilised in the year	(0.5)	(0.5)
At 31 March	1.9	0.9

20. Deferred Income

This is in respect of income received and receivable upon completion of assets under construction and will be utilised over the lifetime of those assets.

	2000 £m	**1999 £m**
At 1 April	40.3	40.4
Received and receivable during the year	1.3	1.2
Released to profit and loss account	(1.3)	(1.3)
At 31 March	40.3	40.3

21. Called up share capital

	2000 £m	1999 £m
Authorised:		
301,050,000 ordinary shares of £1 each (1999 301,050,000)	301.1	301.1
200,000,000 7% preference shares of £1 each (1999 200,000,000)	200.0	200.0
	501.1	501.1
Allotted, called up and fully paid:		
276,050,000 ordinary shares of £1 each (1999 276,050,000)	276.1	276.1
200,000,000 7% preference shares of £1 each (1999 200,000,000)	200.0	200.0
	476.1	476.1

The 7% cumulative preference shares carry a fixed cumulative preference dividend at the rate of 7% per annum, payable ½ yearly in arrears on 31st March and 30th September. The shares have no redemption entitlement. On a winding up, the holders have priority before all other classes of shares to receive repayment of capital plus any arrears of dividend. The holders have no voting rights unless the dividend is in arrears by 6 months or more.

22. Reserves Profit and loss account

	2000 £m	1999 £m
At 1 April	587.9	539.8
Profit retained for the year	70.1	48.1
At 31 March	658.0	587.9

23. Cash flow from operating activities

	2000 £m	1999 £m
Operating profit	152.0	166.4
Depreciation of tangible fixed assets	80.7	76.5
Amounts written off tangible fixed assets	—	6.2
Impairment losses on fixed assets	1.6	—
Amortisation of grants and contributions	(1.3)	(1.3)
Increase/(decrease) in provision for uninsured losses	1.0	(0.2)
Net decrease in stock	2.2	0.5
Net (increase)/decrease in debtors	18.3	(1.9)
Net increase in creditors	4.7	7.6
Decrease in restructuring provisions	(5.9)	(5.8)
Cash flow from operating activities	253.3	248.0

24. Reconciliation of net cash flow to movement in net debt

	2000 £m	1999 £m
Increase in cash in the year	2.2	9.2
Cash inflow from decrease in liquid resources	(34.1)	(61.1)
Cash inflow from increase in debt and lease financing	(63.7)	(85.0)
Increase in net debt in the year	(95.6)	(136.9)
Net debt at 1 April	(776.8)	(639.9)
Net debt at 31 March	(872.4)	(776.8)

25. Analysis of net debt

(a) Movements in the year

	At 31 March 2000 £m	Cash Flow £m	At 1 April 1999 £m
Net cash:			
Cash at bank and in hand	7.3	5.7	1.6
Bank overdraft	(28.8)	(3.5)	(25.3)
	(21.5)	2.2	(23.7)
Liquid resources:			
Current asset investments	37.8	(34.1)	71.9
Debt:			
Finance leases	(265.4)	—	(265.4)
Debts falling due within one year	(108.1)	(71.8)	(36.3)
Debts falling due after one year	(515.2)	8.1	(523.3)
	(888.7)	(63.7)	(825.0)
Net debt	(872.4)	(95.6)	(776.8)

(b) Year end reconciliation

	2000 £m	1999 £m
Cash at bank and in hand	7.3	1.6
Current asset investments	37.8	71.9
Bank overdraft	(28.8)	(25.3)
Finance leases due after one year	(265.4)	(265.4)
Debt due within one year	(108.1)	(36.3)
Debt due after one year	(515.2)	(523.3)
	(872.4)	(776.8)

26. Directors' and officers' loans and transactions

No loans or credit transactions with any directors, officers or connected persons subsisted during the year or were outstanding at the end of the year.

27. Pension schemes

The company participates in a number of pension schemes in the UK. The assets of each pension scheme are held separately from the assets of the group and are administered by trustees. The principal schemes are defined benefit schemes in the UK – the Hyder Water Pension Scheme (HWPS), and the Water Mirror Image Pension Scheme (WMIS).

The pension cost under the Statement of Standard Accounting Practice No. 24 ''Accounting for Pension Costs'' for the HWPS and WMIS has been assessed in accordance with the advice of William M. Mercer Limited, consulting actuaries, using the projected unit method for HWPS and the attained age method for WMIS. For funding purposes the main actuarial assumptions used are based upon investment growth of 6.5% per annum, pay growth of 4.5% per annum and increases to pensions in payment and deferred pensions of 3% per annum. The actuarial value of the assets was taken at 88% of the market value of the assets as at 31 March 1998.

The last actuarial valuations for HWPS and WMIS were carried out as at 31 March 1998 with the market values being £324.6m and £99.9m respectively. Using the assumptions adopted for the Statement of Standard Accounting Practice No. 24 ''Accounting for Pension Costs'', the actuarial value of assets represented 113% for HWPS and 118% for WMIS of the value of the accrued benefits after allowing for expected future earnings increases. In deriving the pension cost under SSAP24 the surpluses in HWPS and WMIS are spread over the future working lifetime of employees. A prepayment of pension costs of £5.1m (1999 £3.6m) is included within prepayments and accrued income (note 12).

The total pension cost for the period was £2.8m (1999 £3.5m).

28. Contingent liabilities

The company has provided guarantees in respect of the principal and interest payments relating to Eurobonds issued by its subsidiary undertaking, Welsh Water Utilities Finance PLC, amounting to £200m (1999 £200m).

The company is also a participant in a cash pooling arrangement operated by National Westminster Bank Plc in the United Kingdom. The company has guaranteed the bank overdraft balances of the participating companies, all of which are fellow subsidiaries, subject to a maximum amount equal to the company's own cash balance with the bank. At 31 March 2000 the overdrafts of fellow subsidiary companies in the cash pooling arrangement amounted to £29.9m (1999 £29.8m).

29. Elan aqueduct

In 1984 Welsh Water Authority entered into a conditional sale and purchase agreement with Severn Trent Water Authority for the sale of the aqueduct and associated works by which the bulk supply to Severn Trent reservoirs is conveyed.

The sum of £31.7m, representing the consideration for the conditional sale, has been invested in a trust fund. The principal function of the fund was to provide an income to Welsh Water Authority, whilst preserving the capital value of the fund in real terms. Welsh Water Authority's interest in this fund was vested in Dŵr Cymru Cyfyngedig under the provisions of the Water Act 1989. The assets of the fund are not included in these financial statements.

30. Related party transactions

In accordance with the exemption afforded by Financial Reporting Standard 8 there is no disclosure in these financial statements of transactions with entities that are part of the Hyder plc group.

31. Immediate and Ultimate holding company

The company's immediate parent is Hyder Utilities (Holdings) Ltd. The ultimate holding company and controlling party is Hyder plc which is registered in England and Wales.

The financial statements of Hyder plc can be obtained from the company secretary of Hyder plc, PO Box 295, Alexandra Gate, Rover Way, Cardiff, CF24 5UE.

FIVE YEAR SUMMARY

	Year ended 31 March				
	2000	**1999**	**1998**	**1997**	**1996**
	£m	**£m**	**£m**	**£m**	**£m**
Turnover	476.9	459.3	444.2	428.5	430.9
Operating profit	152.0	166.4	149.7	168.3	150.7
Profit/(Loss) on disposal of fixed assets	0.3	0.5	1.6	0.9	0.7
Profit on ordinary activities before interest and taxation	152.3	166.9	151.3	169.2	151.4
Net interest payable	(54.3)	(51.9)	(36.2)	(20.2)	(12.8)
Profit on ordinary activities before taxation	98.0	115.0	115.1	149.0	138.6
Taxation	1.1	(8.9)	(9.1)	(2.0)	(15.2)
Profit on ordinary activities after taxation	99.1	106.1	106.0	147.0	123.4
Preference dividends	(14.0)	(14.0)	(7.0)	—	—
Ordinary dividends	(15.0)	(44.0)	(434.0)	(79.0)	(67.0)
Retained profit/(loss) for the year	70.1	48.1	(335.0)	68.0	56.4
Fixed assets	2,144.4	1,980.7	1,796.3	1,606.6	1,450.7
Net current liabilities	(172.0)	(62.6)	26.7	55.0	94.0
Total assets less current liabilities	1,972.4	1,918.1	1,823.0	1,661.6	1,544.7
Creditors: amounts falling due after more than one year	(781.9)	(792.8)	(735.7)	(449.9)	(386.6)
Provisions for liabilities and charges	(56.4)	(61.3)	(71.4)	(60.8)	(75.2)
Net assets	1,134.1	1,064.0	1,015.9	1,150.9	1,082.9
Capital and reserves					
Called up share capital	476.1	476.1	476.1	276.1	276.1
Reserves	658.0	587.9	539.8	874.8	806.8
Equity shareholders' funds	934.1	864.0	815.9	1,150.9	1,082.9
Non-equity shareholders' funds	200.0	200.0	200.0	—	—
Total shareholders' funds	1,134.1	1,064.0	1,015.9	1,150.9	1,082.9

Appendix E

UNAUDITED INTERIM ACCOUNTS OF DCC

Unaudited Profit and Loss Account for the Nine Months Ended 31 December 2000

	2000 £m	1999 £m
Turnover	331.2	354.7
Net operating costs	(210.7)	(245.5)
Operating profit	120.5	109.2
Before exceptional items:		
Continuing operations	120.5	141.1
Exceptional items	—	(31.9)
Operating profit	120.5	109.2
Profit on disposal of fixed assets	0.5	0.1
Profit on ordinary activities before interest	121.0	109.3
Interest receivable	2.0	2.0
Interest payable	(51.3)	(43.1)
Profit on ordinary activities before taxation	71.7	68.2
Taxation	—	(7.6)
Profit on ordinary activities after taxation	71.7	60.6
Dividends on preference shares	(10.5)	(10.5)
Profit attributable to ordinary shareholder	61.2	50.1
Dividends on ordinary shares	—	(5.0)
Retained profit for the period	61.2	45.1

Unaudited Balance Sheet at 31 December 2000

	2000 £m	1999 £m
Fixed assets		
Tangible assets	2,211.1	2,088.5
Investments	0.1	0.1
	2,211.2	2,088.6
Current assets		
Stocks and work in progress	2.1	5.2
Debtors	91.2	84.7
Current asset investments	29.8	26.6
Cash at bank and in hand	0.4	0.2
	123.5	116.7
Current liabilities		
Creditors: amounts falling due within one year	(324.2)	(252.3)
Net current (liabilities)	(200.7)	(135.6)
Total assets less current liabilities	2,010.5	1,953.0
Creditors: amounts falling due after more than one year	(772.6)	(785.9)
Provisions for liabilities and charges	(3.3)	(17.0)
Deferred income	(39.3)	(41.0)
Net assets	1,195.3	1,109.1
Capital and reserves		
Called up share capital	476.1	476.1
Reserves	719.2	633.0
Equity shareholders' funds	995.3	909.1
Non-equity shareholders' funds	200.0	200.0
Total shareholders' funds	1,195.3	1,109.1

Unaudited Cashflow Statement for the Nine Months Ended 31 December 2000

	2000 £m	1999 £m
Cash flow from operating activities	172.4	172.2
Returns on investments and servicing of finance		
Interest received	2.0	2.1
Interest paid	(30.3)	(24.2)
Preference dividends paid	(7.0)	(7.0)
Interest element of finance lease rental payments	(8.2)	(14.0)
	(43.5)	(43.1)
Taxation		
UK corporation tax (paid)/repaid	(3.6)	1.2
Capital expenditure and financial investment		
Purchase of tangible fixed assets	(155.5)	(188.0)
Sale of tangible fixed assets	1.1	0.1
Grants and contributions received	6.9	6.9
	(147.5)	(181.0)
Equity dividends paid	(10.0)	(29.7)
Cash outflow before use of liquid resources and financing	(32.2)	(80.4)
Management of liquid resources		
Net decrease in deposits	8.0	45.6
Financing		
Loan received from parent undertaking	25.0	71.0
Loan repayments	(7.7)	(35.9)
	17.3	35.1
(Decrease)/increase in cash in the period	(6.9)	0.3

Appendix F

PROFORMA BALANCE SHEET OF DCC AS AT 31 DECEMBER 2000

DCC Pro Forma Balance Sheet Adjustments

Balance Sheet at	31-Mar-00	31-Dec-00	Bridge Facility	Loan Repayments	Share buyback	Loan Repayment to Hyder	Issue Costs	Bond Proceeds	Loan to Holdings	Bridge Facility Repaid	Loan Repayments	Reclassification	Property Disposals	Proforma Balance Sheet
	1	2	3	4	5	6	7	8	9	10	11	12	13	14
Fixed assets														
Tangible Assets	2144.3	2211.1											(14.5)	2196.6
Investments	0.1	0.1												0.1
	2144.4	2211.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	(14.5)	2196.7
Current assets														
Stocks and work in progress	3.8	2.1												2.1
Debtors and Prepayments	88.9	91.2					12.6	10.4	450.0					564.2
Current asset investments	37.8	29.8										(28.8)		1.0
Cash at bank and in hand	7.3	0.4	1246.0	(216.7)	(428.7)	(245.0)	(23.5)	1901.3	(450.0)	(1246.0)	(304.8)			233.0
	137.8	123.5	1246.0	(216.7)	(428.7)	(245.0)	(10.9)	1911.7	0.0	(1246.0)	(304.8)	(28.8)		800.3
Current liabilities														
Creditors: amounts falling due within one year	(309.8)	(324.2)	(1246.0)	4.8		125.0				1246.0	15.9	28.8	19.5	(130.2)
Net current assets	(172.0)	(200.7)	0.0	(211.9)	(428.7)	(120.0)	(10.9)	1911.7	0.0	(0.0)	(288.9)	(0.0)	19.5	670.1
Total assets less current liabilities	1972.4	2010.5	0.0	(211.9)	(428.7)	(120.0)	(10.9)	1911.7	0.0	0.0	(288.9)	0.0	5.0	2866.8
Creditors: amounts falling due after more than one year	(781.9)	(772.6)		200.0		120.0		(1911.7)			276.9			(2087.4)
Provisions for liabilities and charges	(16.1)	(3.3)												(3.3)
Deferred Income	(40.3)	(39.3)												(39.3)
Net assets	1134.1	1195.3	0.0	(11.9)	(428.7)	0.0	(10.9)	0.0	0.0	0.0	12.0	0.0	5.0	736.8
Capital and reserves														
Called up share capital:														
Ordinary shares	276.1	276.1			(166.2)									109.9
Preference shares	200.0	200.0												200.0
	476.1	476.1	0.0	0.0	(166.2)	0.0	0.0	0.0	0.0	0.0	0.0	0.0		309.9
Capital Redemption Reserve					166.2									166.2
	476.1	476.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		476.1
Reserves	658.0	719.2		(11.9)	(428.7)		(10.9)				12.0		5.0	260.7
Total shareholders' funds	1134.1	1195.3	0.0	(11.9)	(428.7)	0.0	(10.9)	0.0	0.0	0.0	12.0	0.0	5.0	736.8

Notes

1 As per audited financial statements-see page D5.
2 As per unaudited management accounts approved by DCC Board-see page E2.
3 Drawdowns of £1246m under Bridge Facility Agreement.
4 Repayment of £200m WWUF Sterling Bonds; £11.9m penalties for early repayment, and £4.8m for accrued interest.
5 Share buyback of 166.2 million £1 ordinary shares for £428.7m.
6 Repayment of £1246m loan from Hyder.
7 Issue costs relating to drawdowns of £1246m (see 3 above); £12.6m to be written off future profits.
8 Proceeds from issue of Initial Series, including £10.4m issue costs to be written off future profits.
9 Loan to Holdings for the purchase of 109.9 million £1 ordinary shares and £200m preference shares.
10 Repayment of £1246m under Bridge Facility Agreement (see 3 above).
11 Repayment of European Investment Bank loan and Capital Bank finance lease including £12.0m penalty for early payment and £8.5m accrued interest.
12 Reclassification of Bank overdraft against current asset investments (e.g., cash deposits).
13 Land and property disposals to Hyder for £19.5 million.
14 Proforma balance sheet at 31 December 2000 includes £201m of cash reserves to cover Finance Lease principal repayments (£13m) and future enhancement capital expenditure (£220m).

APPENDIX G

Auditor's report to the members of Dwr Cymru (Financing) Limited

We have audited the financial statements set out on page G-2.

Responsibility

The directors are responsible for preparing the financial statements. This includes responsibility for preparing the financial statements, in accordance with applicable United Kingdom Accounting Standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board and our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the United Kingdom Companies Act. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding director's remuneration and transactions is not disclosed.

Basis of opinion

We conducted our work in accordance with the Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

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

Opinion

In our opinion, the financial statements give a true and fair view of the state of the Company's affairs as at 4 May 2001 and have been properly prepared in accordance with the Companies Act 1985.

PricewaterhouseCoopers
Chartered Accountants and Registered Auditors
4 May 2001

Dwr Cymru (Financing) Limited

Balance Sheet as at 4 May 2001

The balance sheet of the Company as at 4 May 2001 is as follows:

	Notes	£
Current assets		
Cash at bank		30,000
Creditors – accruals (formation costs)	2	(30,000)
		—
Net assets		
Represented by:		
Share capital	3	30,000
Profit & Loss Account	2	(30,000)
		—

Notes to the Balance Sheet as at 4 May 2001

1 Accounting policies

The balance sheet has been prepared in accordance with the historical cost convention and in accordance with applicable United Kingdom accounting standards.

2 Costs

The Company was incorporated in the Cayman Islands as Dwr Cymru (Financing) Limited on 15 February 2001 as an exempted company with limited liability.

The Company has not yet commenced to trade, other than incurring costs in respect of its incorporation, and has not declared or paid a dividend. Accordingly, no profit and loss account is presented.

The costs incurred by the Company in respect of its incorporation will be borne by Dŵr Cymru Cyfyngedig, other than the first £30,000 which will be payable by the Company. All costs incurred up to the date of the financial statements in connection with proposed Bond Issue will be borne by Dŵr Cymru Cyfynygedig.

3 Share capital

The Company was incorporated with an authorised share capital of £50,000, comprising 50,000 Ordinary shares of £1 each. 30,000 Ordinary shares were allotted for cash, and fully paid.

APPENDIX H

Ernst & Young Opinion on DCC Financial Projections

The Directors — 4 May 2001
Dŵr Cymru Cyfyngedig
Plas y Ffynnon
Cambrian Way
Brecon
Powys LD3 7HP

Dear Sirs

We have reviewed the accounting policies and calculations for the illustrative financial projections of Dŵr Cymru Cyfyngedig for each of the four years ending 31 March 2005 set out on pages 165 to 168 of the Information Memorandum dated 4 May 2001.

The illustrative financial projections, which have been prepared under the historical cost convention, should not be regarded as a forecast. They have been prepared, based on the assumptions set out on pages 165 to 168 of the Information Memorandum, to illustrate the possible results of Dŵr Cymru Cyfyngedig if the proposed issue of the Bonds (as defined therein) and associated transactions proceed. Events and circumstances frequently do not occur as originally expected. Because the projections cover a period of four years, the assumptions are more subjective than they would have been if the illustrative financial projections had been for a shorter period. The actual outcome may therefore differ materially from those projected. For these reasons we do not express any opinion either on the validity of the assumptions or on the possibility of the illustrative financial projections being achieved.

Responsibility

The illustrative financial projections included within the Information Memorandum are the responsibility of the Directors of Dŵr Cymru Cyfyngedig. The Directors of Dwr Cymru (Financing) Limited are responsible for the Information Memorandum in which the illustrative financial projections are included.

It is our responsibility to form an opinion on the illustrative financial projections and to report our opinion to you.

Basis of opinion

We planned and performed our work so as to obtain all the information and explanations which we considered necessary in order to provide us with reasonable assurance that the illustrative financial projections, so far as the accounting policies and calculations are concerned, have been properly compiled on the basis stated.

We conducted our work in accordance with the Statements of Investment Circular Reporting Standards issued by the UK Auditing Practices Board and accordingly should not be relied upon as if it had been carried out in accordance with any other standards.

Opinion

In our opinion the illustrative financial projections, so far as the accounting policies and calculations are concerned, have been properly compiled on the basis of the assumptions made by the Directors of Dŵr Cymru Cyfyngedig set out on pages 165 to 168 of the Information Memorandum and have been prepared on a basis consistent with the accounting policies normally adopted by Dŵr Cymru Cyfyngedig.

Yours faithfully

Ernst & Young

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REGISTERED OFFICE OF THE ISSUER

P.O. Box 309, Ugland House
South Church Street
George Town, Grand Cayman
Cayman Islands

REGISTERED OFFICE OF DCC

Plas y Ffynnon
Cambrian Way
Brecon, Powys
Wales LD3 7HP

AUDITORS TO DCC, HOLDINGS, HUH, GLAS, GLAS SECURITIES AND THE ISSUER

PricewaterhouseCoopers
1 Kingsway
Cardiff CF10 3PW

TAX ADVISERS TO DCC, HOLDINGS, HUH AND THE ISSUER

Ernst & Young
1 Lambeth Palace Road
London SE1 7EU

ISSUER SECURITY TRUSTEE, DCC SECURITY TRUSTEE AND BOND TRUSTEE

Bankers Trustee Company Limited
Winchester House
1 Great Winchester Street
London EC2N 2DB

PRINCIPAL PAYING AGENT AND TRANSFER AGENT

Deutsche Bank AG London
Winchester House
1 Great Winchester Street
London EC2N 2DB

REGISTRAR, PAYING AGENT AND TRANSFER AGENT

Deutsche Bank Luxembourg S.A.
2 Boulevard Konrad Adenauer
L-1115 Luxembourg

LEGAL ADVISERS

To the Issuer as to Cayman Islands law

Maples and Calder Europe
7 Princes Street
London EC2R 8AQ

To DCC, Holdings, HUH and the Issuer, as to English law

Allen & Overy
One New Change
London EC4M 9QQ

To Glas and Glas Securities

Linklaters
Linklaters & Alliance
One Silk Street
London EC2Y 8HQ

To MBIA

Clifford Chance Limited Liability Partnership
200 Aldersgate Street
London EC1A 4JJ

To the DCC Security Trustee, the Issuer Security Trustee and the Bond Trustee

Clifford Chance Limited Liability Partnership
200 Aldersgate Street
London EC1A 4JJ

To the Co-Arrangers

Clifford Chance Limited Liability Partnership
200 Aldersgate Street
London EC1A 4JJ

LUXEMBOURG LISTING AGENT

BNP Paribas Luxembourg
10A Boulevard Royal
L-2093 Luxembourg

imprima de bussy — C82223