

# SOUTH STAFFORDSHIRE WATER PLC

*(Incorporated in England and Wales with limited liability under registered number 02662742)*

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## £35,000,000 1.843 PER CENT. INDEX-LINKED BONDS DUE 2051

Issue Price: 100 per cent.

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Application has been made to the Financial Services Authority in its capacity as competent authority under the Financial Services and Markets Act 2000 (the UK Listing Authority) for the £35,000,000 1.843 per cent. Index-Linked Bonds due 2051 (the “**Bonds**”) of South Staffordshire Water plc (the “**Issuer**”) to be admitted to the Official List of the UK Listing Authority and to London Stock Exchange plc (the “**London Stock Exchange**”) for the Bonds to be admitted to trading on the London Stock Exchange’s regulated market. The London Stock Exchange’s regulated market is a regulated market for the purposes of Directive 2004/39/EC (the Markets in Financial Instruments Directive).

Interest on the Bonds (adjusted for indexation) will be payable semi-annually in arrear on 30 June and 30 December in each year at the rate of 1.843 per cent. per annum, the first payment to be made on 30 December 2008, as described under “Terms and Conditions of the Bonds — Interest”. Payments of principal of, and interest and premium (if any) on, the Bonds will be made without withholding or deduction on account of United Kingdom taxes, to the extent described under “Terms and Conditions of the Bonds — Taxation”.

The Bonds will mature on 30 June 2051 and are subject to redemption at the option of the Issuer: (a) in whole but not in part at their outstanding principal amount together with accrued interest (in each case as adjusted for indexation) in the event of certain changes affecting taxes of the United Kingdom; (b) at any time in whole or in part at the amounts set out in Condition 8(c); or (c) upon the occurrence of certain events in relation to the Index (as defined in Condition 6(f)) — See under “Terms and Conditions of the Bonds — Redemption and Purchase”. Upon the occurrence of certain events, as described under “Terms and Conditions of the Bonds — Redemption at the Option of Bondholders”, the holders of the Bonds may require the Issuer to redeem or, at its option, purchase (or procure the purchase of) the Bonds at their principal amount plus any accrued interest (in each case adjusted for indexation).

The Bonds will be issued on 30 June 2008 (the “**Closing Date**”) and will initially be represented by a temporary global bond (the “**Temporary Global Bond**”), without interest coupons, which will be deposited with a common depositary for Euroclear Bank S.A./N.V. (“**Euroclear**”) and Clearstream Banking, société anonyme (“**Clearstream, Luxembourg**”) on or about the Closing Date. Interest in the Temporary Global Bond will be exchangeable for interest in a permanent global bond (the “**Permanent Global Bond**”) and, together with the Temporary Global Bond, the “**Global Bonds**”), without interest coupons, on or after a date which is expected to be 11 August 2008 upon certification as to non-U.S. beneficial ownership. The Permanent Global Bond will be exchangeable for definitive Bonds in bearer form, with interest coupons attached, in the limited circumstances set out in the Permanent Global Bond. Definitive Bonds, if issued, will be issued in bearer form in the denomination of £50,000.

**An investment in the Bonds involves certain risks. Prospective investors should have regard to the risks described under “Risk Factors” on page 6 which may affect the ability of the Issuer to fulfil its obligations in respect of the Bonds.**

Moody’s Investors Service, Limited and Standard & Poor’s Ratings Services, a division of The McGraw-Hill Companies, Inc. are expected to assign ratings of Baa2 and BBB+, respectively, in respect of the Bonds. A security rating is not a recommendation to buy, sell or hold securities and may be subject to revision or withdrawal at any time by the assigning rating organisation.

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BARCLAYS CAPITAL

26 June 2008

*This document comprises a prospectus for the purposes of Article 5.3 of Directive 2003/71/EC (the “Prospectus Directive”).*

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

*This Prospectus is to be read in conjunction with all documents which are deemed to be incorporated herein by reference (as described under “**Documents Incorporated by Reference**”) and shall be read and construed on the basis that such documents are incorporated in and form part of this Prospectus.*

*Market data and certain industry forecasts (where applicable) used throughout this Prospectus have been extracted from information published by the Office of Water Services (“Ofwat”). This information, while believed to be reliable, has not been independently verified, and the Issuer and the Manager do not make any representation as to the accuracy of that information. The Issuer confirms that where the information in this Prospectus has been reproduced from information published by Ofwat, it has been accurately reproduced and that, as far as the Issuer is aware and able to ascertain from information published by Ofwat, no facts have been omitted which would render the reproduced information inaccurate or misleading.*

*This Prospectus does not constitute an offer of, or an invitation by or on behalf of the Issuer or the Manager (as defined under “**Subscription and Sale**”) to subscribe for or purchase, any of the Bonds. This Prospectus does not constitute an offer, and may not be used for the purpose of an offer to, or a solicitation by, anyone in any jurisdiction or in any circumstances in which such offer or solicitation is not authorised or is unlawful.*

*Barclays Bank PLC (the “**Manager**”) and Citicorp Trustee Company Limited (the “**Trustee**”) have not separately verified the information contained herein. Accordingly, no representation, warranty or undertaking, express or implied, is made and no responsibility or liability is accepted by the Manager or the Trustee as to the accuracy or completeness of the information contained or incorporated in this Prospectus or any other information provided by the Issuer in connection with the Bonds or their distribution. The Manager and the Trustee do not accept any liability in relation to the information contained or incorporated by reference in this Prospectus or any other information provided by the Issuer in connection with the Bonds.*

*No person is or has been authorised by the Issuer, the Manager or the Trustee to give any information or to make any representation not contained in or consistent with this Prospectus or any other information supplied by it in connection with the Bonds and, if given or made, such information or representation must not be relied upon as having been authorised by the Issuer, the Manager or the Trustee.*

*This Prospectus is not intended to provide the basis of any credit or other evaluation and should not be considered as a recommendation by the Issuer, the Trustee or the Manager that any recipient of this Prospectus should purchase any of the Bonds. Each investor contemplating purchasing Bonds should make its own independent investigation of the financial condition and affairs, and its own appraisal of the creditworthiness, of the Issuer.*

*Neither the delivery of this Prospectus nor the offering, sale or delivery of any Bonds shall in any circumstances imply that the information contained herein concerning the Issuer is correct at any time subsequent to the date hereof or that any other information supplied in connection with the Bonds is correct as of any time subsequent to the date indicated in the document containing the same. The Manager and the Trustee expressly do not undertake to review the financial condition or the affairs of the Issuer during the life of the Bonds or to advise any investor in the Bonds of any information coming to their attention. Investors should review, inter alia, the most recently published documents incorporated by reference into this Prospectus when deciding whether or not to purchase any Bonds.*

*The distribution of the Prospectus and the offering of the Bonds in certain jurisdictions may be restricted by law. Persons into whose possession this Prospectus comes are required by the Issuer, the Trustee and the Manager 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 any state securities laws, and are subject to U.S. tax law requirements. Subject to certain exceptions, the Bonds may not be offered, sold or delivered within the United States or to U.S. persons. For a further description of certain restrictions on offerings and sales of Bonds and on distribution of this Prospectus, see “Subscription and Sale”.*

*In this Prospectus, references to “£”, “pounds”, “sterling”, “pence” or “p” are to the lawful currency of the United Kingdom and references to a “Member State” are to a Member State of the European Economic Area.*

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IN CONNECTION WITH THE ISSUE OF THE BONDS, BARCLAYS BANK PLC OR ANY PERSON ACTING ON BEHALF OF BARCLAYS BANK PLC MAY OVER-ALLOT BONDS OR EFFECT TRANSACTIONS WITH A VIEW TO SUPPORTING THE MARKET PRICE OF THE BONDS AT A LEVEL HIGHER THAN THAT WHICH MIGHT OTHERWISE PREVAIL AFTER THE CLOSING DATE. HOWEVER THERE IS NO ASSURANCE THAT BARCLAYS BANK PLC (OR PERSONS ACTING ON BEHALF OF BARCLAYS BANK PLC) WILL UNDERTAKE STABILISATION ACTION. ANY STABILISATION ACTION MAY BEGIN ON OR AFTER THE DATE ON WHICH ADEQUATE PUBLIC DISCLOSURE OF THE TERMS OF THE OFFER OF THE BONDS IS MADE AND, IF BEGUN, MAY BE ENDED AT ANY TIME, BUT IT MUST END NO LATER THAN THE EARLIER OF 30 DAYS AFTER THE CLOSING DATE AND 60 DAYS AFTER THE DATE OF THE ALLOTMENT OF THE BONDS. ANY STABILISATION ACTION OR OVER-ALLOTMENT MUST BE CONDUCTED BY BARCLAYS BANK PLC (OR PERSONS ACTING ON BEHALF OF BARCLAYS BANK PLC) IN ACCORDANCE WITH ALL APPLICABLE LAWS AND RULES.

## DOCUMENTS INCORPORATED BY REFERENCE

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The following documents which have previously been published and have been filed with the Financial Services Authority shall be incorporated in, and form part of, this Prospectus:

- (a) the auditors' report and audited annual financial statements of the Issuer for the financial year ended 31 March 2006; and
- (b) the auditors' report and audited annual financial statements of the Issuer for the financial year ended 31 March 2007.

Following the publication of this Prospectus a supplement may be prepared by the Issuer and approved by the UK Listing Authority in accordance with Article 16 of the Prospectus Directive. Statements contained in any such supplement (or contained in any document incorporated by reference therein) shall, to the extent applicable (whether expressly, by implication or otherwise), be deemed to modify or supersede statements contained in this Prospectus or in a document which is incorporated by reference in this Prospectus. Any statement so modified or superseded shall not, except as so modified or superseded, constitute a part of this Prospectus.

Any information which is incorporated by reference in documents which are deemed to be incorporated in, and to form part of, this Prospectus, shall not form part of this Prospectus for the purposes of the Prospectus Directive.

Copies of documents incorporated by reference in this Prospectus can be obtained from the registered office of the Issuer and from the specified offices of the Paying Agent for the time being in London.

The Issuer will, in the event of any significant new factor, material mistake or inaccuracy relating to information included in this Prospectus which is capable of affecting the assessment of the Bonds and which arises or is noted prior to the Issue Date, prepare a supplement to this Prospectus.

## RISK FACTORS

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*The Issuer believes that the following factors may affect its ability to fulfil its obligations under the Bonds. Most of these factors are contingencies which may or may not occur and the Issuer is not in a position to express a view on the likelihood of any such contingency occurring.*

*In addition, factors which are material for the purpose of assessing the market risks associated with the Bonds are also described below.*

*The Issuer believes that the factors described below represent the principal risks inherent in investing in the Bonds, but the inability of the Issuer to pay interest, principal or other amounts on or in connection with any Bonds may occur for other reasons and the Issuer does not represent that the statements below regarding the risks of holding any Bonds are exhaustive. Prospective investors should also read the detailed information set out elsewhere in this Prospectus and analyse all other relevant personal, and market and economic factors as they deem appropriate in order to reach their own views prior to making any investment decision. Capitalised words and expressions defined under Condition 20 of "Terms and Conditions of the Bonds" or elsewhere in this Prospectus have the same meanings in this section.*

### **Factors that may affect the Issuer's ability to fulfil its obligations under the Bonds**

***The turnover, profitability and cash flow of South Staffordshire Water plc (SSW) is substantially influenced by the decisions of Ofwat (including the regulatory targets and price limits), which could adversely affect the profitability or financial condition of SSW.***

The current Periodic Review concludes in 2010 and Ofwat is expected to announce the final outcome of the 2010 to 2015 Periodic Review in late 2009. The 2010 to 2015 Periodic Review may be based upon assumptions by Ofwat that result in the annual limit on price increases and level of allowed returns for SSW being decreased. This includes, but is not limited to, the potential for the current post tax real allowed rate of return of 5.7 per cent. being reduced, which would, in turn, reduce SSW's profitability.

An adverse price determination may occur as a result of a number of factors. There is a risk to ongoing profitability should assumptions taken into account by Ofwat in determining the annual limit on price increases, prove to be incorrect.

If new obligations which have not been taken into account in a Periodic Review lead to an increase in the cost base of SSW, it may not be possible to reflect such increases in prices charged to customers until the next Periodic Review, unless the change in circumstances leading to the increase in cost base can be covered by the interim determination of K ("IDoK") process (described in the following risk factor), and this would have an adverse effect on the business, profitability and cash flow of SSW.

***An application for a tariff adjustment pursuant to an IDoK may not be granted or, if granted, may not provide adequate revenue compensation for SSW***

Under the conditions of the instrument of appointment by the Secretary of State for the Environment appointing SSW as a water undertaker (the "Licence"), an IDoK may be made between Periodic Reviews in specified circumstances, including when a change in circumstances has occurred which has or will have a substantial adverse effect or a substantial favourable effect on the business of that regulated company (a "Substantial Effect Clause"). There can be no assurance that any tariff adjustment will be made pursuant to an IDoK sought by SSW, or that any tariff adjustment made pursuant to such IDoK will provide adequate revenue compensation to SSW and if so, this would have an adverse effect on the business, profitability and cash flow of SSW.

***Until the next Periodic Review, SSW is exposed to revenue loss arising from any deviations in the underlying assumptions used to calculate the RPI+K price cap***

Subject to the provisions covering IDoK applications under the Licence, the RPI+K price cap limits the annual weighted average increase in the standard charges of SSW. This, in turn, is calculated by reference to the "tariff basket" formula, which is constructed so as to provide some compensation in respect of certain unexpected risks (for example, high rateable value customers opting for a meter). However, generally SSW is not protected in respect of each Periodic Review period against revenue loss arising from any deviations from projections during that Periodic Review, including demographic

changes affecting SSW's customer base (for example, SSW is heavily dependent on the continued presence of the manufacturing, brewing and food production industries in its customer base), the loss of a major customer, unexpected movements in volumes of water consumed by customers, or loss through "inset" appointments.

Accordingly, at Periodic Reviews, Ofwat factors into its projections assumptions relating to numbers of customers and volumes consumed. Until the next Periodic Review, SSW will bear the risk that actual numbers of customers and volumes consumed will fall short of the assumptions reflected in the RPI+K price cap. Since actual outturn 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 Periodic Review period may be reflected in such price limits and this could adversely affect the profits of SSW.

***Failure by SSW to deliver its capital investment programme could adversely affect its business, results of operations, profitability or financial condition***

SSW requires significant capital expenditure for additions to, or replacement of, plant and equipment for its water supply and networks. Each Periodic Review takes into account the level of capital expenditure to be incurred during the subsequent five-year price review period and the associated funding costs and operating costs.

In addition, it is important for SSW to ensure that Ofwat is given sufficient information at the time of such Periodic Review to ensure that capital expenditure projections are accurate and that SSW then implements such capital expenditure programme in an efficient manner and in accordance with assumptions made regarding performance so as to remain within the parameters of the Periodic Review determination.

If SSW is unable to deliver its capital investment programme at expected expenditure levels, or is unable to secure the expected level of efficiency savings on its capital investment programme, or if the programme falls behind schedule or contains incorrect assumptions as to the capital investment required, SSW's business, results of operations, profitability or financial condition may be adversely affected due to a need to increase capital expenditure.

***Changes to legislation or unforeseen changes in the water quality requirements may result in a future requirement for further financing***

Changes to legislation or unforeseen changes in the water quality requirements may result in a future requirement for additional funds. There is no commitment in place guaranteeing that such funds required in the future will be available.

***Increases in energy prices, the cost of commodities used by SSW (including chemicals) and/or treatment costs could adversely affect SSW's business, profitability or financial condition***

Energy prices and the cost of chemicals and other substances used by SSW in its treatment processes have increased in recent years. SSW has sought to mitigate the impact of known increases, to the extent that they were not taken into account in the Final Determination, through efficiency savings built into its business plan. However, further increases in energy prices and/or the cost of other commodities could lead to higher operating costs, which could adversely affect SSW's business, profitability or financial condition.

***A deficit in SSW's Water Companies Pension Scheme may require SSW to make additional contributions to the said scheme which could adversely affect SSW's business, profitability or financial condition***

A surplus of £5.7 million existed as at 31 March 2007 on an ongoing FRS 17 accounting basis. However, on alternative valuation methods, for example on a buyout basis, this surplus would be interpreted as a deficit in the scheme. This may require an increase in future contributions by SSW that may not be recognised by Ofwat in future Periodic Reviews, which could adversely affect SSW's business, profitability or financial condition.

In addition, the size of any funding deficit is exposed to movements in the financing markets and long term investment returns may remain lower than the rate assumed by the actuaries in the pension scheme valuations. Therefore, there can be no guarantee that any deficit will not increase over time.

***A change in the rate of inflation could adversely affect SSW's business, profitability or financial condition***

SSW's revenue is linked to the underlying RPI and as such is subject to fluctuations in line with changes in RPI. However, changes in RPI are likely to impact on the operating costs and capital expenditure of SSW (and there is no guarantee that RPI-linked increases in SSW's revenue will necessarily match inflation-driven increases in its operating costs and capital expenditure) and on customers' ability to pay any increased charges.

***A failure to comply with drinking water quality regulation could adversely affect SSW's business, profitability or financial condition***

SSW is under a duty to supply water that is wholesome at the time of supply. "Wholesomeness" is defined by reference to water quality standards and other requirements set out in the Water Supply (Water Quality) Regulations 2000 (SI 2000/3184) (the "**Water Quality Regulations**"). Under the Water Industry Act 1991, the Drinking Water Inspectorate ("**DWI**") is required to take enforcement action against SSW for any breach of water quality standards, or of the monitoring, treatment, record keeping and/or information requirements of the Water Quality Regulations, unless the breach is trivial or unlikely to recur, or SSW has taken immediate remedial action, or it has submitted a legally binding programme of work (the "**undertaking**") to achieve compliance within an acceptable timescale. If there has been such a breach and SSW does not give an undertaking or fails to comply with the terms of the undertaking, the DWI may make a provisional or final enforcement order to secure compliance.

In addition, SSW may be prosecuted and fined if it supplies water that is unfit for human consumption. Any undertakings, enforcement action and prosecutions could materially affect the way that SSW operates, tarnish its reputation and result in the imposition of substantial fines or other costs, each of which could adversely affect SSW's profitability or financial position.

***Environmental risks may adversely affect SSW's business, profitability or financial condition***

SSW is exposed to environmental risks, given the nature of its operations, and environmental situations could arise in the future which could affect its profits and its ability to pay dividends or make other payments to its shareholders. As mentioned below, water supplies may be exposed to pollution, including pollution from the development of naturally occurring compounds or contamination resulting from man-made sources. Should any such pollution or contamination occur in respect of SSW's water supply and it is unable to substitute a water supply from an uncontaminated water source, or to adequately and cost-effectively treat the contaminated water source, there may be an adverse effect on its business profitability or financial position. In addition, SSW could be held liable for human exposure to dangerous substances in its water supplies or other environmental damage. While SSW maintains insurance policies in relation to liabilities likely to be associated with these risks, there can be no guarantee that the costs of any such claims would be fully covered or that such insurance coverage will continue to be available in the future. Moreover, insurance cover is not available at a commercially acceptable premium in respect of gradual contamination.

There can be no assurance as to whether or not existing weather patterns will have an adverse effect on the operations or financial condition of SSW or that existing weather patterns will continue in the future. It is not possible to accurately assess the impact that any climate change may have on the operations or financial condition of SSW.

***Risk of drought***

SSW's water supply is also at risk of water shortages caused by prolonged periods of drought. If there are supply shortfalls caused by prolonged periods of drought, additional costs may be incurred by SSW to provide emergency reinforcement of supplies to areas facing shortage. Restrictions on water use may



adversely affect revenues from metered customers and may, in very extreme circumstances, lead to significant compensation having to be paid to customers who suffer interruptions in supply.

***Disruption of key installations could adversely affect SSW's business, profitability or financial condition***

SSW's two principal treatment works supply approximately 60 per cent. of its average demand. The two principal treatment works, Hampton Loade and Seedy Mill, are therefore key to the ongoing proper operation of the business and, as a result, disruption at one or both of these key installations could adversely affect SSW's profitability or financial condition.

***A significant regulatory action could have a material adverse effect on SSW's business, profitability or financial condition***

The business of SSW is subject to applicable regulations in the UK and EU. In addition, the various environmental protection and health and safety laws and regulations which govern SSW's business establish, amongst other things, standards for drinking water and discharges into the environment. Regulatory authorities may from time to time make enquiries of companies within their jurisdiction regarding compliance with regulations governing the operation of water companies. SSW faces the risk that a regulator or other governmental regulatory body could find that SSW has failed to comply with applicable regulations or has not successfully undertaken corrective action. Regulatory proceedings could then be taken which could result in adverse publicity to, or negative perceptions regarding, SSW as well as diverting management's attention from the day-to-day management of SSW's business. A significant regulatory action could have a material adverse effect on SSW's business, profitability or financial condition.

***Substantial legal liability in the future could have a material adverse effect on SSW's business, profitability or financial condition***

SSW faces the risk of litigation in connection with its business. In general, liability for litigation is difficult to assess or quantify; recovery may be sought for very large and/or indeterminate amounts and the existence and magnitude of liability may remain unknown for substantial periods of time. Substantial legal liability in the future could have a material adverse effect on SSW's business, operations or financial condition.

***Damage, failure or interruption of information systems could have a material adverse effect on SSW's business, operations or financial condition***

SSW's ability to maintain financial controls and provide high-quality customer service to customers depends, in part, on the efficient and uninterrupted operation of its information systems, including its computer systems. Computer systems are potentially vulnerable to damage or interruption from floods, fires, power loss, telecommunication failures and similar events. These information systems may also be subject to sabotage, vandalism and similar misconduct. The same is true of third-party service and software providers depended on by SSW. Further, there is no assurance that these information systems will function as designed. Any damage to or failure of information systems could result in interruptions to SSW's financial controls and customer service. Such interruption could have a material adverse effect on its business, profitability or financial condition.

***SSW may suffer losses from its inability to fully recover customer receivables***

SSW is responsible for the billing, cash collection and debt management activities for its water customers. Under the Water Industry Act 1999, both the disconnection of a water supply for non-payment and the limiting of a water supply with the intention of seeking to enforce payment are prohibited for certain premises (including private dwellings). SSW is therefore exposed to certain risks in respect of non-recovery of customer receivables, which risks may cause its profitability to suffer. Moreover, a general economic downturn in SSW's area of supply could have an adverse impact on SSW's ability to recover customer receivables. There can be no assurance that SSW will not suffer losses from its inability to recover its customer receivables fully.

***Modification or termination of SSW's Licence would have a material adverse impact on SSW's business, profitability or financial condition***

The Licence granted to SSW specifies the geographical areas served and provides SSW with a regional monopoly for the provision of drinking water in those areas. The Licence is subject to conditions and under the Water Industry Act 1991, the conditions may be modified by Ofwat. Any modification to the Licence could have a material impact on SSW. The Water Industry Act 1991 further specifies certain circumstances in which Ofwat could terminate the Licence for all or part of SSW's licensed geographical area. Termination of all or part of the Licence could have a material adverse impact on SSW. Any such modification or termination would have a material adverse impact on SSW's business, profitability or financial condition.

***SSW's sales to non-domestic customers***

Twenty-four per cent. of SSW's regulated water sales for the year ended 31 March 2007 was derived from non-domestic customers, who are susceptible to global, national and regional changes in the economy. A reduction in revenues deriving from non-domestic customers to the extent not anticipated in the price setting process will have an adverse effect on the profits of SSW.

***Hedging***

SSW has in the past, and may in the future, enter into certain hedging arrangements in connection with financing or in the ordinary course of its business. Certain hedging arrangements will exist at the time of issue of the Bonds. Under these hedging arrangements SSW pays annualised sums which in turn may have an adverse effect on its financial position but currently SSW does not consider the payments of these annualised sums to be significant to its cashflow.

**Factors which are material for the purpose of assessing the market risks associated with the Bonds**

***The Bonds may not be a suitable investment for all investors***

Each potential investor in the Bonds must determine the suitability of that investment in light of its own circumstances. In particular, each potential investor should:

- (i) have sufficient knowledge and experience to make a meaningful evaluation of the Bonds, the merits and risks of investing in the Bonds and the information contained or incorporated by reference in this Prospectus or any applicable supplement;
- (ii) have access to, and knowledge of, appropriate analytical tools to evaluate, in the context of its particular financial situation, an investment in the Bonds and the impact the Bonds will have on its overall investment portfolio;
- (iii) have sufficient financial resources and liquidity to bear all of the risks of an investment in the Bonds until the maturity of the Bonds, including Bonds with principal or interest payable in one or more currencies, or where the currency for principal or interest payments is different from the potential investor's currency;
- (iv) understand thoroughly the terms of the Bonds and be familiar with the behaviour of any relevant indices and financial markets; and
- (v) be able to evaluate (either alone or with the help of a financial adviser) possible scenarios for economic, interest rate and other factors that may affect its investment and its ability to bear the applicable risks.

***Risks related to the structure of the Bonds***

During any period when the Issuer may elect to redeem Bonds, the market value of those Bonds generally will not rise substantially above the price at which they can be redeemed. This also may be true prior to the first date on which the Bonds may be redeemed.

The Issuer may be expected to redeem Bonds when its cost of borrowing is lower than the interest rate on the Bonds. At those times, an investor generally would not be able to reinvest the redemption

proceeds at an effective interest rate as high as the interest rate on the Bonds being redeemed and may only be able to do so at a significantly lower rate. Potential investors should consider reinvestment risk in light of other investments available at that time.

#### *The Bonds are Index-Linked*

Both principal and interest for the Bonds are determined by reference to a retail prices index (“RPI”) published by the United Kingdom Office of National Statistics (currently contained in the Monthly Digest of Statistics available online at <http://www.statistics.gov.uk/onlineproducts>). Potential investors should, therefore, be aware that:

- (i) the market price of the Bonds may be volatile;
- (ii) the amount payable at redemption may be less than the principal amount of the Bonds and investors may lose part or all of their investment;
- (iii) RPI may be subject to significant fluctuations that may not correlate with other indices;
- (iv) the timing of changes in RPI may affect the actual yield to investors, even if the average level is consistent with their expectations; and
- (v) the Issuer is permitted to redeem the Bonds early in circumstances in which the Index ceases to be published or is changed fundamentally in a manner that would (in the opinion of an independent Expert) be prejudicial to the Bondholders or the Issuer and no appropriate substitute index (or changes to the Index) can be recommended by that Expert.

#### *Risks related to Bonds generally*

Set out below is a brief description of certain risks relating to the Bonds generally:

##### *Modification, waivers and substitution*

The conditions of the Bonds contain provisions for calling meetings of Bondholders to consider matters affecting their interests generally. These provisions permit defined majorities to bind all Bondholders including Bondholders who did not attend and vote at the relevant meeting and Bondholders who voted in a manner contrary to the majority.

The conditions of the Bonds also provide that the Trustee may, without the consent of Bondholders, agree to (i) any modification of, or to the waiver or authorisation of any breach or proposed breach of, any of the provisions of Bonds or (ii) determine without the consent of the Bondholders that any Event of Default or potential Event of Default shall not be treated as such or (iii) the substitution of another company as principal debtor under any Bonds in place of the Issuer, in the circumstances described in Conditions 12 and 14 of the conditions of the Bonds.

##### *EU Savings Directive*

Under European Council Directive 2003/48/EC on the taxation of savings income (the “**Savings Directive**”), Member States are required to provide to the tax authorities of another Member State details of payments of interest (or similar income) paid by a person within its jurisdiction to an individual or to certain non-corporate entities resident in that other Member State (or of certain other payments secured for their benefit). However, for a transitional period, Belgium, Luxembourg and Austria are instead required to operate a withholding system in relation to such payments (the ending of such transitional period being dependent upon the conclusion of certain other agreements relating to information exchange with certain other countries) unless during such period those countries elect otherwise. A number of other non-EU countries and territories including Switzerland have adopted similar measures (a withholding system in the case of Switzerland).

If a payment were to be made or collected through a Member State which has opted for a withholding system and an amount of, or in respect of, tax were to be withheld from that payment, neither the Issuer nor any Paying Agent nor any other person would be obliged to pay additional amounts with respect to any Bond as a result of the imposition of such withholding tax. If a withholding tax is imposed on

payment made by a Paying Agent, the Issuer will be required to maintain a Paying Agent in a Member State that will not be obliged to withhold or deduct tax pursuant to the Savings Directive.

#### *Change of law*

The conditions of the Bonds are based on English law in effect as at the date of this Prospectus. No assurance can be given as to the impact of any possible judicial decision or change to English law or administrative practice after the date of this Prospectus.

#### ***Risks related to the market generally***

Set out below is a brief description of the principal market risks, including liquidity risk, exchange rate risk, interest rate risk and credit risk:

#### *The secondary market generally*

The Bonds may have no established trading market when issued, and one may never develop. If a market does develop, it may not be very liquid. Therefore, investors may not be able to sell their Bonds easily or at prices that will provide them with the anticipated yield or a yield comparable to similar investments that have a developed secondary market.

#### *Exchange rate risks and exchange controls*

The Issuer will pay principal and interest on the Bonds in Sterling. This presents certain risks relating to currency conversions if an investor's financial activities are denominated principally in a currency or currency unit (the "Investor's Currency") other than Sterling. These include the risk that exchange rates may significantly change (including changes due to devaluation of Sterling or revaluation of the Investor's Currency) and the risk that authorities with jurisdiction over the Investor's Currency may impose or modify exchange controls. An appreciation in the value of the Investor's Currency relative to Sterling would decrease: (1) the Investor's Currency-equivalent yield on the Bonds; (2) the Investor's Currency-equivalent value of the principal payable on the Bonds; and (3) the Investor's Currency-equivalent market value of the Bonds.

Government and monetary authorities may impose (as some have done in the past) exchange controls that could adversely affect an applicable exchange rate. As a result, investors may receive less interest or principal than expected, or no interest or principal.

#### *Credit ratings may not reflect all risks*

One or more independent credit rating agencies may assign credit ratings to the Bonds. The ratings may not reflect the potential impact of all risks related to structure, market, additional factors discussed above, and other factors that may affect the value of the Bonds. A credit rating is not a recommendation to buy, sell or hold securities and may be revised or withdrawn by the rating agency at any time.

#### ***Legal investment considerations may restrict certain investments***

The investment activities of certain investors are subject to legal investment laws and regulations, or review or regulation by certain authorities. Each potential investor should consult its legal advisers to determine whether and to what extent: (1) Bonds are legal investments for it; (2) Bonds can be used as collateral for various types of borrowing; and (3) other restrictions apply to its purchase or pledge of any Bonds. Financial institutions should consult their legal advisers or the appropriate regulators to determine the appropriate treatment of Bonds under any applicable risk-based capital or similar rules.

## TERMS AND CONDITIONS OF THE BONDS

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The following is the text of the Terms and Conditions of the Bonds which (subject to amendment) will be endorsed on each Bond in definitive form if issued:

The £35,000,000 1.843 per cent. Index-Linked Bonds due 2051 (the “**Bonds**”, which expression shall in these Terms and Conditions, unless the context otherwise requires, include any further bonds issued pursuant to Condition 19 and forming a single series with the Bonds) are constituted by a trust deed (the “**Trust Deed**”) dated 30 June 2008 (the “**Closing Date**”) between South Staffordshire Water plc (the “**Issuer**”) and Citicorp Trustee Company Limited (the “**Trustee**”, which expression shall include all persons for the time being the trustee or trustees under the Trust Deed) as trustee for the holders of the Bonds (the “**Bondholders**”). The issue of the Bonds was authorised by a resolution of the board of directors of the Issuer passed on 23 May 2008 appointing an executive committee and a resolution of such executive committee passed on 23 June 2008. Application has been made for the Bonds to be admitted to the Official List of the UK Listing Authority (the “**Official List**”) and to London Stock Exchange plc (the “**London Stock Exchange**”) for such Bonds to be admitted to trading on the London Stock Exchange’s regulated market (the “**Market**”). Admission to the Official List together with admission to the Market constitute official listing on the London Stock Exchange. The statements in these Terms and Conditions include summaries of, and are subject to, the detailed provisions of and definitions in the Trust Deed. Copies of the Trust Deed and of an agency agreement (the “**Paying Agency Agreement**”) dated the Closing Date between the Issuer, Citibank, N.A., London Branch as principal paying agent (the “**Principal Paying Agent**”, which expression shall include any successor in such capacity), the other paying agents named therein (together with the Principal Paying Agent, the “**Paying Agents**”, which expression shall include any additional or successor paying agents) and the Trustee are available for inspection during normal business hours by the Bondholders and the holders of the interest coupons appertaining to the Bonds (the “**Couponholders**” and the “**Coupons**” respectively) at the specified office of each of the Paying Agents. The Bondholders and the Couponholders are entitled to the benefit of, are bound by, and are deemed to have notice of, all the provisions of the Trust Deed and the Paying Agency Agreement.

Unless defined elsewhere in these Terms and Conditions, capitalised words and expressions used in these Terms and Conditions shall have the meanings given to them in Condition 20.

### 1. Form, Denomination and Title

The Bonds are in bearer form, serially numbered, in the denomination of £50,000. Each Bond will have Coupons attached on issue. Title to the Bonds and the Coupons will pass by delivery.

The Issuer, any Paying Agent and the Trustee may (to the fullest extent permitted by applicable laws) deem and treat the holder of any Bond or Coupon as the absolute owner for all purposes (whether or not the Bond or Coupon shall be overdue and notwithstanding any notice of ownership, trust or any interest in it or writing on the Bond or Coupon or any notice of previous loss or theft of the Bond or Coupon).

### 2. Status

The Bonds and the Coupons are direct, unconditional and, subject to the provisions of Condition 3, unsecured obligations of the Issuer and, subject as aforesaid, rank and will rank *pari passu* without any preference among themselves. The payment obligations of the Issuer under the Bonds and the Coupons shall, save for such exceptions as may be provided by applicable laws and subject to Condition 3, at all times rank at least equally with all other outstanding unsecured and unsubordinated obligations of the Issuer, present and future.

### 3. Negative Pledge

So long as any of the Bonds remain outstanding (as defined in the Trust Deed) the Issuer shall not:

- (a) (and the Issuer shall ensure that no other member of the Group will) create or permit to subsist any encumbrance over all or any of its assets, present or future; and

(b) (and the Issuer shall ensure that without the prior written consent of the Trustee no other member of the Group will):

- (i) sell, transfer or otherwise dispose of any of its assets on terms whereby they are or may be leased to or re-acquired by the Issuer or any other member of the Group;
- (ii) sell, transfer or otherwise dispose of any of its receivables on recourse terms; or
- (iii) enter into any other preferential arrangement or transaction having a similar effect,

in circumstances where the arrangement or transaction is entered into primarily as a method of raising Indebtedness for Borrowed Money or of financing the acquisition of an asset. The Trustee may consent to such arrangement or transaction pursuant to Condition 3(b) where such arrangement or transaction is, in the opinion of the Trustee, not materially prejudicial to the interests of the Bondholders.

Condition 3 does not apply in respect of any Permitted Encumbrances.

#### 4. Covenants

(a) *Financial Covenants*

(i) Financial Ratios

The Issuer shall at each Calculation Date:

- (A) maintain an Interest Cover Ratio of at least 1.0:1; and
- (B) maintain a Regulated Asset Ratio of not more than 0.90:1.

(b) *Financial Information Covenants*

(i) General

For so long as any of the Bonds remain outstanding, the Issuer makes the covenants and undertakings set out below in favour of the Trustee for the benefit of the Bondholders.

(ii) Delivery of Accounts

(A) The Issuer shall:

- (i) at all times keep proper books of account and allow the Trustee and any person appointed by the Trustee to whom the Issuer shall have no reasonable objection free access to such books of account at all reasonable times during normal business hours; and
- (ii) as soon as the same become available, but in any event within 120 days after the end of each of its Financial Years (beginning with its current Financial Year) deliver to the Trustee, one copy of its audited unconsolidated and audited consolidated financial statements, if any, to the extent the same are legally required or required by Applicable Accounting Principles for such Financial Year together with the Auditors' reports accompanying such unconsolidated and consolidated financial statements.

(iii) Contents and Certification of Accounts

The Issuer shall procure that the unconsolidated and consolidated financial statements, if any, delivered pursuant to Condition 4(b)(ii)(A) above shall:

- (A) give a true and fair view of the state of its affairs and profits, financial condition and operations as at that date and for the Financial Year then ended; and
- (B) include such financial statements as are required by the applicable laws of England and Wales prepared and (where required) audited using accounting principles, standards and practices consistent with those applied in the preparation of the audited unconsolidated

and audited consolidated financial statements as of and for the previous year (the “**Audited Financial Statements**”) provided that if there have been one or more changes in any such accounting principles, standards and practices, in relation to any such set of unconsolidated and consolidated financial statements, unless notice of such changes appears in the relevant unconsolidated and consolidated financial statements, the Issuer shall notify the Trustee and shall procure that the Auditors confirm to the Trustee that such changes are in accordance with Applicable Accounting Principles.

If any changes to the Applicable Accounting Principles would or would reasonably be expected to result in any of the financial covenants in these Terms and Conditions on the part of the Issuer being more onerous in their effect on the Issuer than they were prior to such changes, then all the relevant methods of calculation of financial covenants in these Terms and Conditions (including, without limitation, the methods of calculation set out in the definitions of “Backward-looking Post Depreciation ICR”, “Cash Flow Forecast”, “Forecast Net Cash Flow”, “Forward-looking Post Depreciation ICR”, “Historic Net Cash Flow” and “Total Net Indebtedness”) shall be modified in such manner as may be agreed in writing by the Issuer and the Trustee (in each case acting reasonably) to ensure that such financial covenants are no more or less onerous in their effect on the Issuer than they were prior to such changes in the Applicable Accounting Principles. For the avoidance of doubt, any such modifications may occur more than once and may occur each time there are any changes to the Applicable Accounting Principles which would or would reasonably be expected to have the effect as aforesaid.

(iv) Investor Report

The Issuer will, as soon as possible and, in any case, within 60 days following any Calculation Date deliver to the Trustee an Investor Report signed on its behalf by an Authorised Signatory.

(v) Other information

- (A) The Issuer will deliver to the Trustee as soon as reasonably practicable after any reasonable request therefor made by the Trustee, a certificate or such other information dealing with such matters as the Trustee may reasonably require to be satisfied or to receive information on for the purposes of the Terms and Conditions and the Trust Deed.
- (B) The Issuer shall deliver to the Trustee two copies of any notice, circular, report, document or other written information which it produces to be sent to its shareholders generally (or any class of them) or its creditors generally other than documents which are of a routine nature.
- (C) The Issuer shall deliver to the Trustee a copy of all material information which would have a Material Adverse Effect which the Issuer supplies to the DGWS save to the extent prohibited by law (at the same time as such is supplied).
- (D) The Issuer shall as soon as reasonably practicable after becoming aware of the same, inform the Trustee of the details of any proposed changes to the Instrument of Appointment, except those changes which are of a minor or technical nature.
- (E) The Issuer shall give to the Trustee (i) within seven days after demand by the Trustee therefor and (ii) (without the necessity for any such demand) promptly after the publication of its audited accounts in respect of each financial period commencing with the financial period ending 31 March, 2008 and in any event not later than 180 days after the end of each such financial period a certificate in or substantially in the form set out in the Trust Deed signed by one director of the Issuer to the effect that as at a date not more than seven days before delivering such certificate (the “**certification date**”) there did not exist and had not existed since the certification date of the previous certificate (or in the case of the first such certificate the date of the Trust Deed) any

Event of Default or any Potential Event of Default (or if such exists or existed specifying the same) and that during the period from and including the certification date of the last such certificate (or in the case of the first such certificate the date of the Trust Deed) to and including the certification date of such certificate the Issuer has complied with all its obligations contained in these Terms and Conditions and the Trust Deed or (if such is not the case) specifying the respects in which it has not complied.

(vi) Auditors' Review

If at any time there appears to be, in the reasonable opinion of the Trustee following consultation with the Issuer, a material discrepancy, inconsistency, omission or error in any of the financial information provided to it pursuant to these Terms and Conditions, the Issuer shall, at its cost, have such financial information reviewed, and if reasonably required by the Trustee (taking into account the costs involved in such an audit) audited by the Auditors and a copy of the Auditors' report in respect thereto shall be delivered to the Trustee. Provided that, prior to the occurrence of a Potential Event of Default or Event of Default, the Trustee shall not be entitled to request the review of such information by the Auditors at the cost of the Issuer on more than one occasion in any calendar year (which shall not restrict the ability of the Trustee to request such a review at its own cost).

(c) *Positive Covenants*

(i) Notification of Events of Default etc.

The Issuer shall notify the Trustee in writing of the occurrence of:

- (A) any Potential Event of Default or Event of Default;
- (B) any event which would reasonably be expected to give rise to an insurance claim in excess of 5 per cent. of Regulated Asset Value;
- (C) any other event which has or would have a Material Adverse Effect,

in each case as soon as reasonably practicable upon becoming aware of such event (which notice shall describe in detail the relevant circumstances giving rise thereto) and shall, at the same time as delivering each Investor Report, confirm to the Trustee that no such event has occurred or, if such event has occurred, give details of such event.

(ii) Material Litigation

The Issuer shall as soon as reasonably practicable notify the Trustee in writing (which notice shall describe in detail the relevant circumstances giving rise thereto) of:

- (A) any pending or (to the best of the Issuer's knowledge and belief) threatened prosecution, statutory notice (including any enforcement or prohibition notice), claim, formal investigation or other proceeding or suit served on the Issuer ("**Proceeding**") including any alleged breach thereof which individually or in aggregate would have a Material Adverse Effect and the Issuer shall, as soon as practicable, notify the Trustee in writing of any Proceeding which had previously not been considered would have a Material Adverse Effect if at any time the circumstances of that Proceeding change such that it would have a Material Adverse Effect; and
- (B) any non-compliance with any law which would have a Material Adverse Effect, and set out the action to be taken with respect to such matters.

(iii) Conduct of Business

The Issuer shall operate, maintain and conduct its business in a safe, proper and efficient manner in all material respects, and, in accordance with:

- (A) the Instrument of Appointment;



- (B) its Memorandum and Articles of Association; and
  - (C) Good Industry Practice (taking its business as a whole).
- (iv) Compliance with Laws  
The Issuer shall use all reasonable endeavours to comply in all material respects with all laws and regulations applicable to it.
- (v) Permitted Business  
The Issuer shall ensure that the nature of its business is limited to the Permitted Business.
- (vi) Ratings covenant  
The Issuer shall, unless it has previously redeemed in full or purchased and cancelled the Bonds, use its reasonable endeavours to ensure that it maintains an Investment Grade rating of the Bonds issued by both Rating Agencies. In addition, the Issuer agrees to co-operate with the Rating Agencies in connection with any reasonable request for information in respect of the maintenance of an Investment Grade rating and with any review of the Permitted Business which may be undertaken by either of the Rating Agencies after the date hereof.
- (d) *Negative Covenants*
- (i) Merger  
The Issuer shall not except with the prior written consent of the Trustee (such consent not to be unreasonably withheld or delayed), enter into any amalgamation, demerger, merger, consolidation, corporate reconstruction or any such like arrangement.
  - (ii) Transfer of Appointment  
The Issuer shall not except with the prior written consent of the Trustee, propose or agree to any scheme of transfer as defined in Schedule 2 to the Act unless an independent financial adviser selected by the Issuer and approved by the Trustee has certified to the Trustee either that any such scheme of transfer will not be materially prejudicial to the interests of the Bondholders or that no scheme of transfer which is materially less prejudicial to such interests is likely to be forthcoming in a reasonable period. The cost and expenses of any independent financial adviser shall be borne by the Issuer.
  - (iii) Restrictions on Transactions with Affiliates  
The Issuer shall not, except with the prior written consent of the Trustee (such consent not to be unreasonably withheld or delayed), enter into any transaction or agreement with any Affiliate save (a) on the basis that such transaction or agreement shall have fair and commercially reasonable terms no less favourable to the Issuer than could reasonably be expected to be obtained in a comparable arm's length transaction with a person which is not an Affiliate or (b) transactions or agreements with Affiliates at cost (provided such costs are commercially reasonable and standard) (for the avoidance of doubt this Condition 4(d)(iii) does not restrict the Issuer from entering into transactions which are permitted in accordance with its Instrument of Appointment).
  - (iv) Guarantees and Indemnities  
The Issuer shall not, except with the prior written consent of the Trustee, grant any credit, give any indemnity or make any loan to or for the benefit of any person other than (i) in the ordinary course of business or (ii) loans to employees, or (iii) payments made in accordance with Condition 4(d)(vii) below, in all cases to the extent permitted by the Instrument of Appointment.

(v) Amendments

The Issuer shall not except with the prior written consent of the Trustee:

- (A) agree to any amendment to, or variation or waiver or termination or assignment of, its Articles of Association or its Memorandum of Association (save for any amendment which is of a minor or technical nature or is to cure a manifest error) or enter into any agreement with its shareholders which, in either case, has or would have a Material Adverse Effect;
- (B) agree to any amendment to the Instrument of Appointment which has or would have a Material Adverse Effect.

(vi) Subsidiaries

The Issuer shall not acquire or have any additional subsidiaries, except with the prior written consent of the Trustee (such consent not to be unreasonably withheld or delayed).

(vii) Relevant Payments

(A) The Issuer shall not, except with the prior written consent of the Trustee or as otherwise permitted by Condition 4(d)(iii) (*Restrictions on Transactions with Affiliates*) above, pay, make or declare, or otherwise make any payment in respect of, any Relevant Payment unless:

- (i) if a notice to terminate the Instrument of Appointment has been served, an independent financial adviser (selected by the Issuer with the approval of the Trustee) has certified to the Trustee that a transfer scheme as defined in Schedule 2 of the Act has been established or other satisfactory security has been provided and that such transfer scheme as defined in Schedule 2 of the Act will not be materially prejudicial to the interests of the Bondholders. The costs and expenses incurred of any independent financial adviser shall be borne by the Issuer;
- (ii) as at the Calculation Date immediately following the applicable Relevant Payment assuming that the proposed Relevant Payment had been made:
  - (A) no Potential Event of Default or Event of Default would occur;
  - (B) the ICR would be greater than or equal to 1.50:1 in any Calculation Period up to and including the Final Forecast Date; and
  - (C) the RAR would be less than or equal to 0.85:1 at that Calculation Date and any Calculation Date up to and including the Final Forecast Date;
- (iii) there is no failure to pay any outstanding principal or interest or any other sum due and payable from the Issuer in relation to any Indebtedness at the time of the making of the Relevant Payment, in currency and in the manner specified required and if there is such failure (in the case of a sum other than principal or interest) it has continued unremedied for a period of (i) three Business Days after the relevant due date or (ii) any applicable grace period, whichever is the later for payment of such sum; and
- (iv) the Issuer is able to certify to the Trustee that in respect of any Relevant Payments to be paid, made or declared, it has complied with the criteria set out in Condition 4(d)(vii)(A)(ii); and

(B) The Issuer may not make a Relevant Payment if on the date upon which such Relevant Payment is proposed to be made (i) the rating of the Bonds by either of the Rating Agencies has fallen below Investment Grade or will fall below Investment Grade when the Relevant Payment is made, or the Bonds have been placed on credit watch with negative implications and it is reasonably likely that such rating will fall below Investment Grade, unless the Trustee confirms to the Issuer that it is satisfied that the

making of such Relevant Payment would not negatively affect the rating of the Bonds by any of the Rating Agencies; or (ii) the Bonds are not rated by both of the Ratings Agencies; or (iii) an Event of Default or Potential Event of Default has arisen or is subsisting or would arise or subsist as a result of the making of such Relevant Payment.

- (C) The Issuer may not make a Relevant Payment (except with the consent of the Trustee) if the final reading of draft legislation in the House of Lords or the House of Commons has commenced (whichever occurs later) and such draft legislation is in substantially the same form as prior readings and the enactment of such legislation would have a Material Adverse Effect (taking into account the regulatory regime applicable to the Business of the Issuer at such time).

For the avoidance of doubt, a Relevant Payment may be made on any date, subject to this Condition 4(d)(vii) (and any related provisions).

- (viii) The Trustee may give its prior written consent pursuant to Condition (d)(i)-(vii) where to give such consent would not, in the opinion of the Trustee, be materially prejudicial to the interests of the Bondholders.

## 5. Interest

Each Bond bears interest from (and including) the Closing Date at the rate of 1.843 per cent. per annum. The interest amount shall be adjusted for indexation in accordance with Condition 6 and shall be payable semi-annually in arrear on 30 June and 30 December in each year (each an “**Interest Payment Date**”), the first such payment to be made on 30 December 2008. All amounts of interest due on each Bond will be rounded to the nearest one penny (half a penny being rounded upwards).

Each Bond will cease to bear interest from its due date for redemption unless, upon due presentation, payment of the principal in respect of such Bond is improperly withheld or refused or unless default is otherwise made in respect of such payment, in which event interest shall continue to accrue as provided in the Trust Deed.

## 6. Indexation

- (a) *Determination of Rate of Interest and calculation of Interest Amounts*

The amount (the “**Interest Amount**”) of interest payable on each Bond for any Interest Period (which expression shall, in these Terms and Conditions, mean the period from (and including) an Interest Payment Date (or the Closing Date) to (but excluding) the next (or first) Interest Payment Date) will be calculated by the Principal Paying Agent at, or as soon as practicable after, each time at which the Rate of Interest is capable of being determined, by: (A) applying the Rate of Interest to the principal amount of such Bond; (B) multiplying the resulting amount by the Day Count Fraction; and (C) rounding the resulting figure to the nearest one penny (half a penny being rounded upwards).

The “**Day Count Fraction**” is a fraction: (a) the numerator of which is the number of days from and including the most recent Interest Payment Date (or Closing Date if such period is before the first scheduled Interest Payment Date) to but excluding the next Interest Payment Date or, if earlier, the date of payment; and (b) the denominator of which is two times the number of days (including the first and excluding the last) in the Interest Period.

- (b) The Principal Paying Agent shall cause each Interest Amount to be published in accordance with Condition 16 as soon as possible after its determination date but in no event later than the second Business Day thereafter.

- (c) *Determination or Calculation by Trustee*

If for any reason the Principal Paying Agent at any time after the Closing Date defaults in its obligation to determine or calculate:

- (A) the Rate of Interest;
- (B) any Interest Amount in accordance with paragraph (a) above;
- (C) the Final Redemption Amount (as defined below); or
- (D) the Early Redemption Amount (as defined below),

the Trustee shall determine or calculate the same, in its absolute discretion (having such regard as it shall think fit to the foregoing provisions of this Condition 6 and, as applicable, to Condition 8), and in such manner as it shall deem fair and reasonable in all the circumstances and each such determination or calculation shall be deemed to have been made by the Principal Paying Agent and in so doing the Trustee shall be entitled to seek (at the expense of the Issuer) and rely upon advice from any reputable investment bank or other reputable and suitably qualified expert deemed appropriate by the Trustee for such purpose.

(d) *Notifications, etc. to be Final*

All notifications, opinions, determinations, certificates, calculations, quotations and decisions given, expressed, made or obtained for the purposes of the provisions of this Condition 6, whether by the Principal Paying Agent or the Trustee, will (in the absence of wilful default, bad faith or manifest error) be binding on the Issuer, the Trustee and all Bondholders and Couponholders and (in the absence of wilful default and bad faith) no liability to the Issuer or the Bondholders or the Couponholders shall attach to the Principal Paying Agent or, if applicable, the Trustee in connection with the exercise or non-exercise by any of them of their powers, duties and discretions under this Condition.

(e) *Indexation of principal*

The amount payable pursuant to Condition 8(a) (the “**Final Redemption Amount**”) and any amounts payable pursuant to Condition 8(b), 8(c), 8(d), 9 or 12 (each an “**Early Redemption Amount**”) shall be the principal amount (or, in the case of 8(c), the Redemption Price, if applicable) of the Bonds multiplied by the Index Ratio applicable to the month in which the Final Redemption Amount or the Early Redemption Amount (as the case may be) becomes payable.

The Principal Paying Agent will calculate such Final Redemption Amount or Early Redemption Amount (as the case may be) as soon as practicable after each time such amount is capable of being determined. The Principal Paying Agent will as soon as practicable thereafter notify the Issuer, the Trustee and (if required by any applicable law or regulation) any stock exchange on which the Bonds are for the time being listed of the amount thereof and cause notice thereof to be published in accordance with Condition 16.

Any reference in these Terms and Conditions to principal in respect of the Bonds shall be deemed also to refer to the Final Redemption Amount and the Early Redemption Amount.

(f) *Definitions*

For the purposes of these Conditions:

“**Base Index Figure**” means 213.87742 (being the Index Figure applicable to 30 June 2008 (that is the Index published in April 2008 and relating to March 2008);

“**Expert**” means an independent investment bank or other expert in London appointed by the Issuer and approved by the Trustee or (failing such appointment or approval within 10 days) appointed by the Trustee (at the expense of the Issuer);

“**Index**” means, in relation to any Index Calculation Date, subject as provided in Conditions 6(g) and 8(d) below, the United Kingdom General Index of Retail Prices (for all items) as published by the United Kingdom Office for National Statistics (January 1987=100) (currently contained in the Monthly Digest of Statistics) and applicable to that Index Calculation Date or, if that index is not published for any Index Calculation Date, any substituted index or index figures published by the

United Kingdom Office for National Statistics or the comparable index which replaces the United Kingdom General Index of Retail Prices (for all items) for the purpose of calculating the amount payable on repayment of the Reference Gilt;

“**Index Calculation Date**” means any Interest Payment Date or any other date on which a payment under the Bonds falls due to be made;

Any reference to the “**Index Figure**” applicable to a particular Index Calculation Date shall, subject as provided in Condition 6(g) below, be calculated in accordance with the following formula:

$$RPI_{m-3} + \frac{(\text{nth Day of Index Calculation Date} - 1)}{(\text{Days in month of Index Calculation Date})} \times (RPI_{m-2} - RPI_{m-3})$$

and rounded to five decimal places (0.000005 being rounded upwards) and where:

$RPI_{m-3}$  means the Index Figure for the first day of the month that is three months prior to the month in which the payment falls due; and

$RPI_{m-2}$  means the Index Figure for the first day of the month that is two months prior to the month in which the payment falls due;

“**Index Ratio**” applicable to any Index Calculation Date means the Index Figure applicable to such date divided by the Base Index Figure and rounded to five decimal places (0.000005 being rounded upwards);

the “**Rate of Interest**” applicable to any amount payable shall be 1.843 per cent. per annum multiplied by the Index Ratio applicable to the relevant Index Calculation Date and rounded to four decimal places (0.00005 being rounded upwards); and

“**Reference Gilt**” means the 0.75 per cent. Index-Linked Treasury Stock due 2047 (or, if such stock is not in existence, such other index-linked stock issued by or on behalf of HM Government as the Issuer, on the advice of three brokers and/or gilt edged market makers (or such other three persons operating in the gilt edged market as the Issuer, after consultation with the Trustee, may select (each an “**Indexation Adviser**”)), may consider to be the most appropriate reference government stock for the Bonds).

(g) *Changes in circumstances affecting the Index*

(i) Change in base

If at any time the Index is changed by the substitution of a new base for it, then with effect from (and including) the calendar month for which that substitution takes effect:

(A) the definition of Index in Condition 6(f) shall be deemed to refer to the new date or month in substitution for January 1987 (or, as the case may be, for such other date or month as may have been substituted for it) and references to the Index Figure applicable shall be construed accordingly; and

(B) the definition of Base Index Figure in Condition 6(f) shall be amended to mean the product of the then applicable Base Index Figure and the Index immediately following such substitution, divided by the Index immediately prior to such substitution.

(ii) Cessation of or fundamental changes to the Index

If the Index ceases to be published or any change is made to it which, in the opinion of an Expert, constitutes a fundamental change in the rules governing the Index and the change would, in the opinion of the Expert, be detrimental to the interests of the Issuer or the Bondholders and if, within 30 days after its appointment (or such longer period as the Trustee may approve), the Expert recommends for the purposes of the Bonds one or more adjustments to the Index or a substitute index (with or without adjustments), then provided that such adjustments or substitute index (as the case may be) are not materially detrimental (in the opinion of the Expert) either to the interests of the Issuer or the interests of the

Bondholders, as compared to the interests of the Issuer and the Bondholders (as the case may be) as they would have been had the Index continued to be published or such fundamental change in the rules governing the Index not been made, the Index shall be adjusted as so recommended or (as the case may be) shall be replaced by the substitute index so recommended (as so adjusted, if so recommended) and references in these Terms and Conditions to the Index shall be construed accordingly and the Issuer shall notify the Bondholders of the adjustments to the Index or the introduction of the substitute index (with or without adjustments) in accordance with Condition 16. Any Expert so appointed shall act as an expert and not as an arbiter and all fees, costs and expenses of the Expert and of the Issuer and the Trustee in connection with such appointment shall be borne by the Issuer.

If any payment in respect of the Bonds is due to be made after the cessation or changes referred to in the preceding paragraph but before any such adjustment to, or replacement of, the Index takes effect, the Issuer shall (if the Index Figure applicable (or deemed applicable) to the relevant Index Calculation Date is not available in accordance with the provisions of Condition 6(g)) make a provisional payment on the basis that the Index Figure applicable to the relevant Index Calculation Date is the Index last published. In that event (also referred to below as a “**provisional payment**”) and the Trustee on the advice of the Expert subsequently determining that the relevant circumstances fall within this Condition (g)(ii), then:

- (A) except in the case of a payment on redemption of the Bonds, if the sum which would have been payable if such adjustments or such substitute index had been in effect on the due date for such provisional payment is greater or less than the amount of such provisional payment, the interest payable on the Bonds on the Interest Payment Date next succeeding the last date by which the Issuer and Trustee receive such recommendation shall be increased or reduced (as the case may be) to reflect the amount by which such provisional payment of interest fell short of, or (as the case may be) exceeded, the interest which would have been payable on the Bonds if such adjustments or such substituted index had been in effect on that date; or
- (B) in the case of a payment of principal or interest on redemption of the Bonds, no subsequent adjustment to amounts paid will be made.

(iii) Trustee

The Trustee shall be entitled to assume that no cessation of or change to the Index has occurred until informed otherwise by the Issuer and will not be responsible for identifying or appointing an Expert save as provided in these Terms and Conditions and shall be entitled to rely absolutely on the advice of any Expert and shall not be responsible for any costs or losses incurred thereby.

## 7. Payments

Payments of principal and interest in respect of the Bonds will be made against presentation and surrender (or, in the case of part payment only, endorsement) of the Bonds, except that payments of interest due on an Interest Payment Date will be made against presentation and surrender (or, in the case of part payment only, endorsement) of the relevant Coupons, in each case at the specified office of any of the Paying Agents.

Payments will be made at the specified office of any Paying Agent, at the option of the holder, by sterling cheque drawn on, or by transfer to a sterling account maintained by the payee with, a bank in London subject in all cases to any applicable fiscal or other laws and regulations, but without prejudice to the provisions of Condition 10. No commissions or expenses shall be charged to the Bondholders or the Couponholders in respect of such payments.

Each Bond should be presented for payment (including exercise of the Bondholders' option pursuant to Condition 9) together with all relative unmatured Coupons (being Coupons which would otherwise fall due for payment after the relevant due date for payment or, as the case may be, the Put Date (as defined in Condition 9(c))). Upon the date on which any Bond becomes due and repayable, all unmatured Coupons appertaining to the Bond (whether or not attached) shall become void and no payment shall be made in respect of such Coupons.

A holder shall be entitled to present a Bond or Coupon for payment only on a Presentation Date and shall not be entitled to any further interest or other payment if a Presentation Date falls after the due date.

The names of the initial Paying Agents and their initial specified offices are set out at the end of these Terms and Conditions. The Issuer reserves the right, subject to the prior written approval of the Trustee, at any time to vary or terminate the appointment of any Paying Agent and to appoint additional or other Paying Agents provided that:

- (a) there will at all times be a Principal Paying Agent;
- (b) there will at all times be at least one Paying Agent (which may be the Principal Paying Agent) having its specified office in a European city which, so long as the Bonds are admitted to official listing on the London Stock Exchange, shall be London or such other place as the UK Listing Authority may approve; and
- (c) the Issuer ensures that it maintains a Paying Agent in a Member State of the European Union that is not obliged to withhold or deduct tax pursuant to any law implementing or complying with, or introduced in order to conform to, European Council Directive 2003/48/EC on the taxation of savings income.

Notice of any termination or appointment and of any changes in specified offices will be given to the Bondholders promptly by the Issuer in accordance with Condition 16.

## **8. Redemption and Purchase**

- (a) Unless previously redeemed or purchased and cancelled as provided below, each Bond will be redeemed by the Issuer at its principal amount (subject to adjustment for indexation in accordance with Condition 6) on 30 June 2051.
- (b) If, as a result of any change in, or amendment to, the laws or regulations of the United Kingdom or any political sub-division of, or any authority in or of, the United Kingdom having power to tax, or any change in the application or official interpretation of such laws or regulations, which change or amendment becomes effective after the Closing Date, the Issuer has or will become obliged to pay additional amounts as provided or referred to in Condition 10 (and such amendment or change has been evidenced by the delivery by the Issuer to the Trustee (who shall, in the absence of manifest error, accept such certificate as sufficient evidence thereof) of a certificate signed by two directors of the Issuer stating that such amendment or change has occurred (irrespective of whether such amendment or change is then effective), describing the facts leading thereto and stating that such obligation cannot be avoided by the Issuer taking reasonable measures available to it), the Issuer may, at its option, on any Interest Payment Date, having given not less than 30 nor more than 60 days' notice to the Bondholders in accordance with Condition 16 (which notice shall be irrevocable), redeem all, but not some only, of the Bonds (other than any Bonds in respect of which a notice has been given pursuant to Condition 8(c)) at their principal amount together with interest (if any) accrued to but excluding the date of redemption (each subject to adjustment for indexation in accordance with Condition 6), provided that no notice of redemption shall be given earlier than 90 days before the earliest date on which the Issuer would be required to pay such additional amounts were a payment in respect of the Bonds then due.
- (c) The Issuer may at its option, on any Interest Payment Date, having given not less than 30 nor more than 90 days' notice to the Bondholders in accordance with Condition 16 (which notice shall be

irrevocable), redeem the Bonds in whole or in part (but, if in part, in a principal amount of £5,000,000 or integral multiples thereof) at the price which shall be the higher of the following:

- (i) their principal amount (subject to adjustment for indexation in accordance with Condition 6); and
- (ii) that price (the “**Redemption Price**”), expressed as a percentage rounded to three decimal places (0.0005 being rounded upwards), at which the Gross Redemption Yield on the Bonds, if they were to be purchased at such price on the second dealing day prior to the publication of the notice of redemption, would be equal to the Gross Redemption Yield on such dealing day of the 0.75 per cent. Index-Linked Treasury Stock 2047 or, if such stock is no longer in issue, of such other HM Government stock as the Trustee, with the advice of three Indexation Advisers, shall determine to be appropriate (the “**Reference Stock**”) on the basis of the middle market price of the Reference Stock prevailing at or about 3.00 p.m. (London time) on such dealing day, as determined by Barclays Bank PLC (or such other person(s) as the Trustee may approve). Any reference in these Terms and Conditions to principal shall, where applicable, be deemed to be a reference to the Redemption Price. The “**Gross Redemption Yield**” on the Bonds and the Reference Stock will be expressed as a percentage and will be calculated on the basis set out by the United Kingdom Debt Management Office in the paper “*Formulae for calculating Gilt Prices from Yields*” page 12, 3rd edition published 16 March 2006 (as supplemented, amended or replaced from time to time) or on such other basis as the Trustee may approve,

together with interest (if any) accrued to but excluding the date of redemption and adjusted for indexation in accordance with Condition 6.

Notices of redemption will specify the date fixed for redemption, the applicable redemption price and, in the case of partial redemption, the serial numbers of the Bonds called for redemption, the serial numbers of any Bonds previously called for redemption and not presented for payment and the aggregate principal amount of the Bonds to remain outstanding after redemption. Any partial redemption of the Bonds shall be on the basis of selection by drawings (the method of such drawings to be approved by the Trustee).

(d) *Redemption for Indexation Reasons*

- (i) If the Index ceases to be published or any change is made to it which, in the opinion of an Expert, constitutes a fundamental change in the rules governing the Index and the change would, in the opinion of the Expert, be detrimental to the interests of the Bondholders and if the Expert fails within 30 days after its appointment (or such longer period as the Trustee may approve), or states to the Issuer and the Trustee that it is unable, to recommend for the purposes of the Bonds any adjustments to the Index or any substitute index (with or without adjustments) as described in Condition 6(g)(ii), the Issuer shall, within 14 days after the expiry of such period or (as the case may be) after the date of such statement, give notice (which shall be irrevocable and shall state the date fixed for redemption) to redeem the Bonds then outstanding on the next Interest Payment Date (other than any Bonds in respect of which a notice has been given pursuant to Condition 8(c)), at a price equal to their principal amount multiplied by the Index Ratio applicable to the relevant Index Calculation Date, together with accrued interest (subject to adjustment for indexation in accordance with Condition 6).
- (ii) If the Index ceases to be published or any change is made to it which, in the opinion of an Expert, constitutes a fundamental change in the rules governing the Index and the change would, in the opinion of the Expert, be detrimental to the interests of the Issuer and if the Expert fails within 30 days after its appointment (or such longer period as the Trustee considers reasonable), or states to the Issuer and the Trustee that it is unable, to recommend for the purposes of the Bonds any adjustments to the Index or any substitute index (with or without adjustments) as described in Condition 6(g)(ii), the Issuer may at its option, within 14 days after the expiry of such period or (as the case may be) after the date



of such statement, give notice (which shall be irrevocable and shall state the date fixed for redemption) to redeem the Bonds then outstanding on the next Interest Payment Date, at a price equal to their principal amount multiplied by the Index Ratio applicable to the relevant Index Calculation Date, together with accrued interest (subject to adjustment for indexation in accordance with Condition 6).

- (e) The Issuer, any Subsidiary of the Issuer or the Parent may at any time purchase Bonds (together with unmatured Coupons appertaining thereto) in any manner and at any price. If purchases are made by tender, tenders must be available to all Bondholders alike. The Bonds so purchased, while held by or on behalf of the Issuer, any Subsidiary of the Issuer or the Parent, in each case as the beneficial owner, shall not entitle the holder to vote at any meetings of the Bondholders and shall be deemed not to be outstanding for the purposes of Conditions 9(b), 12, 13 or 17(a) or otherwise as provided in the Trust Deed.
- (f) All Bonds which are redeemed by the Issuer will forthwith be cancelled (together with all relative unmatured Coupons attached to the Bonds or surrendered with the Bonds) and may not be reissued or resold. Bonds purchased by the Issuer, any Subsidiary of the Issuer or the Parent may be held or reissued or resold or surrendered for cancellation, unless purchased pursuant to Condition 9, in which case such Bonds (together with all relative unmatured Coupons attached to the Bonds or surrendered with the Bonds) will forthwith be cancelled as aforesaid.

## 9. Redemption at the Option of Bondholders

- (a) If, at any time while any of the Bonds remains outstanding:
  - (i) the Instrument of Appointment is terminated except in respect of such part of its area as is the subject of an appointment or variation by virtue of section 7(4)(b) or (bb) of the Water Industry Act; or
  - (ii) a Restructuring Event occurs and (subject as provided below):
    - (A) within the Restructuring Period, either:
      - (i) if at the time such Restructuring Event occurs there are Rated Securities, a Rating Downgrade in respect of such Restructuring Event also occurs; or
      - (ii) if at such time there are no Rated Securities, a Negative Rating Event in respect of such Restructuring Event also occurs; and
    - (B) an Independent Financial Adviser shall have certified in writing to the Issuer and the Trustee that such Restructuring Event is, in its opinion, materially prejudicial to the interests of the Bondholders (a “**Negative Certification**”),

then, unless at any time the Issuer shall have given a notice under Condition 8(b), 8(c) or 8(d) in respect of all of the Bonds, the holder of each Bond will, upon the giving of a Put Event Notice (as defined below), have the option (the “**Put Option**”) to require the Issuer to redeem or, at the option of the Issuer, purchase (or procure the purchase of) that Bond on the Put Date (as defined below), at its principal amount together with (or, where purchased, together with an amount equal to) interest (if any) accrued to (but excluding) the Put Date (each adjusted for indexation in accordance with Condition 6).

If, at any time while any of the Bonds remains outstanding, a Restructuring Event occurs and prior to the commencement of or during the Restructuring Period an Independent Financial Adviser shall have certified in writing to the Issuer and the Trustee that such Restructuring Event will not be or is not, in its opinion, materially prejudicial to the interests of the Bondholders, the foregoing provisions shall cease to have any further effect in relation to such Restructuring Event.

A Restructuring Event shall be deemed not to be materially prejudicial to the interests of the Bondholders if, notwithstanding the occurrence of a Rating Downgrade or a Negative Rating Event, the rating assigned to the Rated Securities by any Rating Agency is subsequently increased to, or, as the case may be, there is assigned to the Bonds or other unsecured and unsubordinated

debt of the Issuer (or of any Subsidiary of the Issuer which, in any such case, is guaranteed on an unsecured and unsubordinated basis by the Issuer) having an initial maturity of five years or more by any Rating Agency, an Investment Grade rating prior to any Negative Certification being issued.

Any certification by an Independent Financial Adviser as aforesaid as to whether or not, in its opinion, any Restructuring Event is materially prejudicial to the interests of the Bondholders shall, in the absence of manifest error, be conclusive and binding on the Trustee, the Issuer and the Bondholders.

- (b) Promptly upon, and in any event within 14 days after, the Issuer becoming aware that a Put Event has occurred, the Issuer shall, and if so requested in writing by the holders of at least one quarter in principal amount of the Bonds then outstanding the Trustee shall, give notice (a “**Put Event Notice**”) to the Bondholders in accordance with Condition 16 specifying the nature of the Put Event and the procedure for exercising the Put Option.
- (c) To exercise the Put Option, the holder of a Bond must deliver such Bond to the specified office of any Paying Agent, on a day which is a Business Day in London and in the place of such specified office falling within the period (the “**Put Period**”) of 45 days after that on which a Put Event Notice is given, accompanied by a duly completed and signed notice of exercise in the form (for the time being current) obtainable from any specified office of any Paying Agent (a “**Put Notice**”) and in which the holder may specify a bank account complying with the requirements of Condition 7 to which payment is to be made under this Condition 9. Each Bond should be delivered together with all Coupons appertaining thereto maturing after the day (the “**Put Date**”) being the fifteenth day after the date of expiry of the Put Period. Upon the Put Date, all unmatured Coupons appertaining to the Bond (whether or not attached) shall become void and no payment shall be made in respect of such Coupons. The Paying Agent to which such Bond and Put Notice are delivered shall issue to the Bondholder concerned a non-transferable receipt in respect of the Bond so delivered. Payment in respect of any Bond so delivered shall be made, if the holder duly specifies an account with a bank in London in the Put Notice to which payment is to be made, on the Put Date by transfer to that bank account and, in every other case, on or after the Put Date in each case against presentation and surrender or (as the case may be) endorsement of such receipt at any specified office of any Paying Agent, subject in any such case as provided in Condition 7. A Put Notice, once given, shall be irrevocable. For the purposes of these Terms and Conditions and the Trust Deed, receipts issued pursuant to this Condition 9 shall be treated as if they were Bonds. The Issuer shall redeem or, at the option of the Issuer, purchase (or procure the purchase of) the relevant Bond on the applicable Put Date unless previously redeemed or purchased.
- (d) A Rating Downgrade or a Negative Rating Event or a non-investment grade rating shall be deemed not to have occurred as a result or in respect of a Restructuring Event if the Rating Agency making the relevant reduction in rating or, where applicable, declining to assign a rating of at least Investment Grade does not announce or publicly confirm or inform the Trustee in writing at its request that the reduction or, where applicable, declining to assign a rating of at least Investment Grade was the result, in whole or in part, of any event or circumstance comprised in or arising as a result of the applicable Restructuring Event.
- (e) The Trust Deed provides that the Trustee is under no obligation to ascertain whether a termination of the Instrument of Appointment, a Restructuring Event, a Rating Downgrade, a Negative Rating Event or any event which could lead to the occurrence of or could constitute a Restructuring Event has occurred and until it shall have actual knowledge or express notice pursuant to the Trust Deed to the contrary the Trustee may assume that no such termination, Restructuring Event, Rating Downgrade, Negative Rating Event or such other event has occurred. The Trust Deed also provides that in determining whether or not a Restructuring Event has occurred, the Trustee may rely solely on an opinion given in a certificate signed by two directors of the Issuer.

## 10. Taxation

All payments in respect of the Bonds and the Coupons shall be made free and clear of, and without withholding or deduction for, or on account of, any present or future taxes, duties, assessments or

governmental charges of whatever nature (“**Taxes**”) imposed or levied by or on behalf of the United Kingdom, or any political sub-division of, or any authority in or of, the United Kingdom having power to tax, unless the withholding or deduction of such Taxes is required by law. In the event that such withholding or deduction of such Taxes is required by law, the Issuer will pay such additional amounts as may be necessary in order that the net amounts received by the Bondholders and Couponholders after the withholding or deduction shall equal the respective amounts which would have been receivable in respect of the Bonds or, as the case may be, Coupons in the absence of the withholding or deduction, except that no additional amounts shall be payable in relation to any payment in respect of any Bond or Coupon:

- (a) presented for payment by or on behalf of, a holder who is liable to such Taxes in respect of the Bond or Coupon by reason of his having some connection with the United Kingdom other than the mere holding of the Bond or Coupon; or
- (b) presented for payment more than 30 days after the Relevant Date except to the extent that a holder would have been entitled to additional amounts on presenting the same for payment on the last day of such period of 30 days, assuming, whether or not such is in fact the case, such last day to be a Presentation Date; or
- (c) to, or to a third party on behalf of, a holder who would not be liable or subject to the withholding or deduction by making a declaration of beneficial ownership of the Bond or Coupon or of non-residence or other similar claim for exemption to the relevant tax authority or paying agent or any other relevant person; or
- (d) where such withholding or deduction is imposed on a payment to an individual and is required to be made pursuant to any law implementing or complying with, or introduced in order to conform to, European Council Directive 2003/48/EC on the taxation of savings income; or
- (e) presented for payment by or on behalf of a holder who would be able to avoid such withholding or deduction by presenting the relevant Bond or Coupon to another Paying Agent in a Member State of the European Union.

As used herein, “**Relevant Date**” means the date on which the payment first becomes due but, if the full amount of the money payable has not been received in London by the Principal Paying Agent or the Trustee on or before the due date, it means the date on which, the full amount of the money having been so received, notice to that effect shall have been duly given to the Bondholders by the Issuer in accordance with Condition 16.

Any reference in these Terms and Conditions to any amounts in respect of the Bonds shall be deemed also to refer to any additional amounts which may be payable under this Condition or under any undertakings given in addition to, or in substitution for, this Condition pursuant to the Trust Deed.

## **11. Prescription**

Claims against the Issuer in respect of principal and interest shall be prescribed and become void unless the relevant Bond or Coupon is presented for payment within periods of 10 years (in the case of principal) and five years (in the case of interest) from the Relevant Date in respect thereof.

## **12. Events of Default**

The Trustee at its absolute discretion may, and if so requested in writing by the holders of at least one-quarter in principal amount of the Bonds then outstanding or if so directed by an Extraordinary Resolution of the Bondholders shall, subject, in each case, to being indemnified and/or secured to its satisfaction (but, in the case of the happening of any of the events mentioned in sub-paragraphs (e), (g), (k) and (n) below, only if the Trustee shall have certified in writing to the Issuer that such event is, in its opinion, materially prejudicial to the interests of the Bondholders), give notice to the Issuer that the Bonds are, and they shall accordingly thereby forthwith become, immediately due and repayable at their principal amount together with accrued interest (in each case, adjusted for indexation in accordance

with Condition 6) (as provided in the Trust Deed) if any of the following events (each an “Event of Default”) shall have occurred (unless such event has been remedied to the satisfaction of the Trustee):

(a) *Failure to Pay*

if default is made for a period of 7 Business Days or more in the payment of any principal of or interest on the Bonds or in the payment of the purchase price due in respect of any Bond pursuant to Condition 9. Notwithstanding the above, a failure to pay principal or interest caused solely by an administrative or technical error shall not be an Event of Default provided such payment is made within 1 Business Day of the due date for payment of such sum; or

(b) *Covenants*

if the Issuer fails:

- (i) to observe or perform any of its obligations under Conditions 3 (*Negative Pledge*), 4(c)(i) (*Notification of Events of Default etc.*), 4(d)(ii) (*Transfer of Appointment*) and 4(d)(vii) (*Relevant Payments*) and, in the case of a failure capable of being remedied, such failure is not so remedied within seven days after notice of such failure has been given to the Issuer by the Trustee; or
- (ii) to observe or perform any of its other obligations under the Bonds or the Trust Deed and, in the case of a failure capable of being remedied, such failure is not so remedied within 30 days after notice of such failure has been given to the Issuer by the Trustee, and such failure would have a Material Adverse Effect.

(c) *Ratios*

If on any Calculation Date:

- (i) the ICR in respect of the immediately preceding Calculation Period or the next following Calculation Period is or is expected to be below 1.0:1;
- (ii) the Regulated Asset Ratio in respect of the relevant Calculation Date and any Calculation Date falling in the immediately following Calculation Period, is or is expected to be greater than 0.90:1; or
- (iii) where a Periodic Review falls or is subsisting during a Calculation Period, the RAR for the next twelve month period based on the best information available at the relevant time is or is expected to be greater than 0.90:1.

(d) *Illegality*

At any time it is or it becomes unlawful for the Issuer to perform or comply with any or all of its obligations under the Terms and Conditions or the Trust Deed or any of its obligations thereunder are not, or are claimed by the Issuer not to be, or cease to be, legal, valid and binding and the absence of compliance with such obligation has or would have a Material Adverse Effect.

(e) *Appointment of Receiver, Legal Process*

An encumbrancer takes possession of, or a trustee, special administrator or administrative or other receiver or similar officer is appointed in respect of, all of the business or assets of the Issuer, or any part of the business or assets in excess of 3 per cent. of RAV, or distress or any form of execution is levied or enforced upon or sued out against any such assets and is not discharged within 30 days of being levied, enforced or sued out.

(f) *Insolvency*

The Issuer is adjudicated by a competent court, or admits in writing that it is unable to pay its debts within the meaning of Section 123(1)(a) or Section 123(1)(e) of the Insolvency Act 1986.

For the purposes of this paragraph, Section 123(1)(a) of the Insolvency Act 1986 shall have effect as if for “£750” there was substituted “0.15 per cent. of RAV”.

(g) *Composition*

The Issuer makes any arrangement or composition with, or any assignment for the benefit of, its creditors generally or convenes a meeting of its creditors for the purpose of considering any such arrangement, composition or assignment.

(h) *Administration, Winding Up and Special Administration*

A petition is presented, or a meeting is convened for the purpose of considering a resolution or other steps are taken for making an administration order against or for the winding up of the Issuer or for the appointment of a liquidator, receiver, administrator, special administrator, administrative receiver or similar official of it or any or all of its revenues or assets or a petition is presented under Section 24 of the Act in respect of the Issuer or an administration order or a winding up order is made against the Issuer (other than (i) proceedings which the Issuer believes, in good faith, are frivolous or vexatious in nature and which are discharged within 30 days or (ii) as part of a solvent reorganisation with the prior written consent of the Trustee or as sanctioned by an Extraordinary Resolution of the Bondholders).

(i) *Special Administration*

A special administration order (as such term is defined in the Act) is made in respect of the Issuer under the Act.

(j) *Analogous Proceedings*

Anything which has an analogous effect to any of the events specified in Condition 12(e) (*Appointment of Receiver, Legal Process*), Condition 12(f) (*Insolvency*), Condition 12(g) (*Composition*), Condition 12(h) (*Administration, Winding Up and Special Administration*) or Condition 12(i) (*Special Administration*) occurs in respect of the Issuer under the laws of any other applicable jurisdiction.

(k) *Issuer Cross Acceleration*

Any Indebtedness for Borrowed Money of the Issuer (individually or in the aggregate), in excess of 3 per cent. of RAV, is declared to be or otherwise becomes due and payable prior to its specified maturity by reason of default by the Issuer.

(l) *Change of Business*

The Issuer ceases or threatens to cease to carry on the Business it carries on at the date hereof (other than as permitted by these Terms and Conditions or the Trust Deed).

(m) *Repudiation*

The Issuer repudiates any of these Terms and Conditions or the Trust Deed or does or causes to be done any act or thing evidencing an intention to repudiate any of these Terms and Conditions or the Trust Deed.

(n) *Material Proceedings*

Any litigation against the Issuer or its assets or revenues results in judgment (being both final and without the opportunity for the Issuer to appeal against it) being passed against the Issuer which has or would have a Material Adverse Effect.

### **13. Enforcement**

The Trustee may at any time, at its absolute discretion and without notice, take such proceedings against the Issuer or any other action as it may think fit to enforce the provisions of the Trust Deed, these Terms and Conditions, the Bonds and the Coupons but it shall not be bound to take any proceedings or any other action in relation to the Trust Deed, these Terms and Conditions, the Bonds or the Coupons unless (a) it shall have been so directed by an Extraordinary Resolution of the Bondholders or so requested in writing by the holders of at least one-quarter in principal amount of the Bonds then outstanding, and (b) it shall have been indemnified and/or secured to its satisfaction. No Bondholder or Couponholder shall be entitled to proceed directly against the Issuer unless the Trustee, having become bound so to proceed, fails so to do within a reasonable period and such failure shall be continuing.

### **14. Substitution**

The Trustee may, without the consent of the Bondholders or Couponholders, agree with the Issuer to the substitution in place of the Issuer (or of any previous substitute or substitutes under this Condition) as the principal debtor under the Bonds, the Coupons and the Trust Deed of any Subsidiary of the Issuer subject to (a) the Trustee being satisfied that the interests of the Bondholders will not be materially prejudiced by the substitution and (b) certain other conditions set out in the Trust Deed being complied with.

### **15. Replacement of Bonds and Coupons**

If any Bond or Coupon be lost, stolen, mutilated, defaced or destroyed, it may be replaced at the specified office of the Principal Paying Agent subject to all applicable laws and stock exchange requirements, upon payment by the claimant of the expenses incurred in connection with the replacement and on such terms as to evidence and indemnity as the Issuer may reasonably require. Mutilated or defaced Bonds or Coupons must be surrendered before replacements will be issued.

### **16. Notices**

All notices to the Bondholders will be valid if published in a leading English language daily newspaper published in London (which is expected to be the *Financial Times*) or, if in the opinion of the Trustee such publication shall not be practicable, in an English language daily newspaper with general circulation in Europe. The Issuer shall also ensure that notices are only published in a manner which complies with the rules and regulations of any stock exchange or relevant authority on which the Bonds are for the time being listed. Any notice shall be deemed to have been given on the date of publication or, if so published more than once, on the date of the first publication. If publication as provided above is not practicable, notice will be given in such other manner, and shall be deemed to have been given on such date, as the Trustee may approve. Couponholders will be deemed for all purposes to have notice of the contents of any notice given to the Bondholders in accordance with this Condition.

The Issuer shall procure that all communications, notifications, reports and authorisations and other documents which are to be provided to the Trustee under these Terms and Conditions, the Trust Deed or the Bonds are provided in English.

### **17. Meetings of Bondholders, Modification, Waiver and Authorisation**

(a) The Trust Deed contains provisions for convening meetings of the Bondholders to consider any matter affecting their interests, including the modification by Extraordinary Resolution of any of these Terms and Conditions or any of the provisions of the Trust Deed. The quorum at any meeting for passing an Extraordinary Resolution will be one or more persons present holding or representing a clear majority in principal amount of the Bonds for the time being outstanding, or at any such adjourned meeting one or more persons present whatever the principal amount of the Bonds held or represented by him or them, except that at any meeting the business of which includes modification of certain of the provisions of these Terms and Conditions and certain of the provisions of the Trust Deed, the necessary quorum for passing an Extraordinary Resolution will be

one or more persons present holding or representing not less than two-thirds, or at any such adjourned meeting not less than one-third, of the principal amount of the Bonds for the time being outstanding. An Extraordinary Resolution passed at any meeting of the Bondholders will be binding on all Bondholders, whether or not they are present at the meeting, and on all Couponholders.

- (b) The Trustee may agree, without the consent of the Bondholders or Couponholders, to any modification of, or to the waiver or authorisation of any breach or proposed breach of, any of these Terms and Conditions or any of the provisions of the Trust Deed, or determine, without any such consent as aforesaid, that any Event of Default or Potential Event of Default shall not be treated as such (provided that, in any such case, it is not, in the opinion of the Trustee, materially prejudicial to the interests of the Bondholders) or to any modification which is of a formal, minor or technical nature or to correct a manifest or an error which is, in the opinion of the Trustee, proven.
- (c) In connection with the exercise by it of any of its trusts, powers, authorities and discretions (including, without limitation, any modification, waiver, authorisation, determination or substitution), the Trustee shall have regard to the general interests of the Bondholders as a class but shall not have regard to any interests arising from circumstances particular to individual Bondholders and, in particular but without limitation, shall not have regard to the consequences of any such exercise 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 or any political sub-division thereof and the Trustee shall not be entitled to require, nor shall any Bondholder or Couponholder be entitled to claim, from the Issuer, the Trustee or any other person, any indemnification or payment in respect of any tax consequence of any such exercise upon individual Bondholders or Couponholders except to the extent already provided for in Condition 10 and/or any undertaking given in addition to, or in substitution for, Condition 10 pursuant to the Trust Deed.
- (d) Any modification, waiver or authorisation referred to in paragraph (b) above and any substitution under Condition 14 shall be binding on the Bondholders and the Couponholders and, unless the Trustee agrees otherwise, any such modification or substitution shall be notified by the Issuer to the Bondholders as soon as practicable thereafter in accordance with Condition 16.

## **18. Indemnification of the Trustee**

The Trust Deed contains provisions for the indemnification of the Trustee and for its relief from responsibility, including provisions relieving it from taking action unless indemnified and/or secured to its satisfaction. The Trustee or any of its Affiliates is entitled to enter into business transactions with the Issuer and any entity related to the Issuer without accounting for any profit. The Trustee may rely without liability to Bondholders on a certificate signed by two directors of the Issuer or a report of the Auditors, whether or not addressed to it and whether or not the directors or Auditors, as the case may be, have any liability to it in respect of the same.

## **19. Further Issues**

The Issuer is at liberty from time to time without the consent of the Bondholders or Couponholders to create and issue further bonds or notes either (a) ranking *pari passu* in all respects (or in all respects save for the first payment of interest thereon) and so that the same shall be consolidated and form a single series with the outstanding bonds or notes of any series (including the Bonds) constituted by the Trust Deed or any deed supplemental to it or (b) upon such terms as to ranking, interest, conversion, redemption and otherwise as the Issuer may determine at the time of the issue. Any further bonds or notes which are to form a single series with the outstanding bonds or notes of any series (including the Bonds) constituted by the Trust Deed or any deed supplemental to it shall, and any other further bonds or notes may (with the consent of the Trustee), be constituted by a deed supplemental to the Trust Deed.

## 20. Definitions

For the purposes of these Terms and Conditions:

“**Acceptable Bank**” means a bank or trust company which has a rating of A or A2 or higher (or equivalent rating) issued by one of the Rating Agencies;

“**Acceptable Letter of Credit**” means a letter of credit which:

- (a) shall be issued in favour of the Issuer by a bank which at all times shall be a Qualifying Bank;
- (b) has a residual maturity of not less than 3 months; and
- (c) is in full force and effect,

provided that if at any time the issuer of any such Acceptable Letter of Credit ceases to be a Qualifying Bank, the relevant letter of credit shall not cease to be an Acceptable Letter of Credit until the date which is one month after the Issuer becomes aware that the issuer ceases to be a Qualifying Bank;

“**Act**” means the Water Industry Act 1991;

“**Affiliate**” means, in relation to any person, a Subsidiary of that person or a Holding Company of that person or any other Subsidiary of that Holding Company;

“**Applicable Accounting Principles**” means accounting principles, standards and practices generally accepted in the United Kingdom as applied from time to time to any entity carrying on the Business;

“**Appointed Business**” means the appointed business of a “relevant undertaker” (as that term is defined by the Act);

“**Appointed Expenses**” means the operating expenses of the Appointed Business (excluding, for the avoidance of doubt, any capital expenditure) as shown in the Issuer’s Financial Statements in respect of the relevant period;

“**Auditors**” means the auditors for the time being of the Issuer, who are at 26 June 2008 Deloitte & Touche LLP, Chartered Accountants or, if they are unable or unwilling to carry out any action requested of them under the Terms and Conditions or the Trust Deed, such other firm of accountants as may be nominated by the Issuer (with the prior written approval of the Trustee, such approval not to be unreasonably withheld or delayed) for the purpose or, failing such nomination or approval, as may be nominated by the Trustee;

“**Authorised Investments**” means:

- (a) securities issued by the government of the United Kingdom;
- (b) demand or time deposits, certificates of deposit and short-term unsecured debt obligations, including commercial paper, provided that the issuing entity or, if such investment is guaranteed, the guaranteeing entity, is rated the Minimum Short-term Rating and (if the relevant Authorised Investments have an original maturity in excess of one year) Minimum Long-term Rating;
- (c) money market funds provided that they comply with the Minimum Short-term Rating; and
- (d) any other obligations provided that in each case the relevant investment has the Minimum Short-term Rating or (if the relevant Authorised Investments have an original maturity in excess of one year) the Minimum Long-term Rating and in each case is either denominated in sterling or (following redenomination after the UK becomes a participating member state) euro;

“**Authorised Signatory**” or “**Authorised Signatories**” means, in relation to the Issuer and any communication to be made or document to be executed or certified by the Issuer, at any time, any person or persons:

- (a) who is/are at such time duly authorised by a resolution of the board of directors (or a duly authorised committee thereof) of the Issuer or by virtue of his/their appointment by the Issuer to a particular office to make such communication or to execute or certify such document on behalf of the Issuer; and



- (b) in respect of whom the Trustee has received a certificate of a director or the secretary of the Issuer setting out the name/s and signature/s of such person or persons and confirming such person's or persons' authority so to act, and in respect of whom no notice has been received by the Trustee from the Issuer to the effect that such person or persons is or are no longer an Authorised Signatory or Authorised Signatories for the Issuer;

**“Backward-looking Post Depreciation ICR”** or **“Backward-looking PDICR”** means, in relation to a Calculation Date, the ratio of:

- (a) Historic Net Cash Flow less CCD and IRC for the Calculation Period ending on or most recently prior to such Calculation Date; to
- (b) Historic Debt Service for the Calculation Period ending on or most recently prior to such Calculation Date,

and in respect of the determination of (b) above, only the net payments made or received under any swap, collar, option, cap, floor or other derivative or hedging instrument shall be taken into account;

**“Business”** means the business of a water or water and waste water undertaker (as that term is defined in the Act and the Instrument of Appointment) in England and Wales;

**“Business Day”** means a day (other than a Saturday or Sunday) on which banks and foreign exchange markets are open for business in London and, in the case of a Presentation Date and any specified place, means a day (other than a Saturday or Sunday) on which banks and foreign exchange markets are open in such place;

**“Calculation Date”** means 31 March 2008 and thereafter 31 March and 30 September in each year until the final Interest Payment Date;

**“Calculation Period”** means each period of 12 months commencing on 1 April in each year;

**“Cash and Cash Equivalents”** means, at any time the aggregate of the amounts represented by:

- (a) any cash on deposit with any Acceptable Bank;
- (b) any Acceptable Letter of Credit; and
- (c) any Authorised Investment,

in each case, to which the Issuer is beneficially entitled at that time and which is capable of being applied against its obligations under the Bonds and the Trust Deed;

**“Cash Flow Forecast”** means a forecast of revenues (including investment income, the net proceeds of asset disposals, the proceeds of loss of anticipated revenue and loss of revenue (business interruption and delay in start up) insurance, Tax rebates and projected changes in forecast Total Net Indebtedness) and expenditure of the Issuer for each Calculation Period from the date of such forecast to the next water charges review date (the first such review date being 31 March 2010) prepared and delivered in accordance with the terms of the Terms and Conditions and the Trust Deed;

**“CCD”** means current cost depreciation as determined by OFWAT in the latest regulatory determination or draft determination, indexed with the Retail Price Index in accordance with Condition 6;

**“Date Prior”** means at any time the date which is one day before the next Periodic Review under and as defined in the Instrument of Appointment;

**“DGWS”** means the board of directors of Ofwat or any successor thereto;

**“Event of Default”** means any event described as such in Condition 12;

**“Final Forecast Date”** means the later of (a) the Date Prior and (b) the last day of the Calculation Period falling on or immediately prior to the date two years after the most recent Calculation Date;

**“Finance Leases”** means any lease or hire purchase contract which would, in accordance with generally accepted accounting standards in the United Kingdom, be treated as a finance or capital lease;

**“Financial Statements”** means:

- (a) the most recent audited unconsolidated annual financial statements of the Issuer; and
  - (b) the most recent audited consolidated annual financial statements of the Issuer, if any,
- (as the context requires) and in each case, delivered to the Trustee pursuant to the Trust Deed;

**“Financial Year”** means the period of 12 months ending on 31 March in each year or such other period as may be approved by the Trustee.

**“Forecast Net Cash Flow”** means in relation to any period an amount equal to the aggregate of:

- (a) the projected operating profit of the Issuer (but adding back depreciation, amortisation and the infrastructure renewals charge); plus
- (b) projected interest income of the Issuer,

(as such terms are used in, and each calculated in accordance with the methodology used in, the Issuer’s Financial Statements);

**“Forward-looking Post Depreciation ICR”** or **“Forward-looking PDICR”** means, in relation to a Calculation Date, the ratio calculated in respect of each Calculation Period ending after such Calculation Date, up to and including the Final Forecast Date or such other period expressly stated, of:

- (a) Forecast Net Cash Flow less CCD and IRC for such Calculation Period; to
- (b) Projected Debt Service for such Calculation Period,

and in respect of the determination of (b) above, only the net payments projected to be made or received under any swap, collar, option, cap, floor or other derivative or hedging instrument shall be taken into account;

**“Good Industry Practice”** means the standards, practices, methods and procedures as practised in the United Kingdom conforming to all applicable laws and that degree of skill, diligence, prudence and foresight which would reasonably be expected from a skilled and experienced person undertaking all or part of the Business under the same or similar circumstances having regard, without limitation, to the regulatory pricing allowances in the water and sewerage industry in the United Kingdom at the relevant time;

**“Group”** means the Issuer and its Subsidiaries, if any, for the time being;

**“Historic Debt Service”** means, in relation to any Calculation Date, the aggregate of interest (adjusted for indexation where relevant in accordance with Condition 6 or any agreement entered into by the Issuer which provides for the payment of interest) due and payable on all Indebtedness for Borrowed Money (for the avoidance of doubt excluding any indexation) during the Calculation Period ending on or most recently prior to such Calculation Date (such period to be extended or shortened, if necessary, to ensure it includes only two Interest Payment Dates);

**“Historic Net Cash Flow”** means, in relation to any period, an amount equal to the aggregate of:

- (a) the actual operating profit of the Issuer (but adding back depreciation, amortisation and the infrastructure renewals charge); plus
- (b) interest income of the Issuer,

(as such terms are used in, and each calculated in accordance with the methodology used in, the Issuer’s Financial Statements or the Issuer’s annual return, in each case which relate to the relevant period);

**“Holding Company”** means, in relation to a company or corporation, any other company or corporation in respect of which it is a Subsidiary;

**“Indebtedness”** means any obligation (whether incurred as principal or as surety) for the payment or repayment of money whether present or future, actual or contingent;

**“Indebtedness for Borrowed Money”** means any Indebtedness of the Issuer for or in respect of:

- (a) money borrowed or raised (whether or not for cash);
- (b) amounts raised by acceptance under any acceptance credit facility;
- (c) amounts raised under any note purchase facility;
- (d) amounts payable in respect of Finance Leases;
- (e) amounts payable for assets or services, the payment of which is deferred for a period in excess of 90 days after the date of the relevant invoice and the purpose of the arrangements is to raise finance;
- (f) redeemable preference shares, to the extent that the same are capable of redemption (whether on maturity or at the option of the Issuer or the holder thereof) prior to the date falling one week after the final Interest Payment Date;
- (g) net termination amounts which become due and payable under any swap, option, cap, collar, floor or other derivative or hedging instrument;
- (h) any Third Party Guarantee;
- (i) loan stock, loan notes or bonds; and
- (j) amounts raised under any other transaction (including any forward sale, sale of receivables, securitisation or purchase agreement) having the commercial effect of a borrowing;

**“Independent Financial Adviser”** means an independent financial adviser appointed by the Issuer and approved by the Trustee or, if the Issuer shall not have appointed such an adviser within 7 days after becoming aware of the occurrence of a Restructuring Event and the Trustee is indemnified to its satisfaction against the costs of such adviser, appointed by the Trustee;

**“Instrument of Appointment”** means the Instrument of Appointment dated August 1989 made under Sections 11 and 14 of the Water Act 1989 (as in effect from 1 July 1994) as subsequently modified and varied by the DGWS under sections 11 to 17 of the Act, appointing the Issuer as a water undertaker;

**“Interest Cover Ratio”** or **“ICR”** means the Backward-looking Post Depreciation ICR and the Forward-looking Post Depreciation ICR;

**“Investment Grade”** means a rating of at least “BBB-” by S&P and “Baa3” by Moody’s;

**“Investor Report”** means the report of the Issuer to be delivered to the Trustee in accordance with these Terms and Conditions and the Trust Deed;

**“IRC”** means the infrastructure renewals charge as determined by OFWAT in the latest regulatory determination or draft determination, inflated as appropriate;

**“K”** has the meaning provided in the Instrument of Appointment;

**“Loan Finance Documents”** means the loan facility agreement between the Issuer, Artesian Finance III plc and The Royal Bank of Scotland plc dated 20 December 2005;

**“Material Adverse Effect”** means the effect of any event or circumstance which is or is likely to be materially adverse to:

- (a) the ability of the Issuer to perform or comply with any of its obligations under the Instrument of Appointment or the Act or to carry on the Business generally; or
- (b) the ability of the Issuer to perform or comply with any of its payment or other material obligations under these Terms and Conditions and the Trust Deed;

**“Minimum Long-term Rating”** means, in respect of any person, such person’s long-term unsecured debt obligations being rated, in the case of Moody’s, “Aa2” and in the case of S&P, “AA-”;

**“Minimum Short-term Rating”** means, in respect of any person, such person’s short-term unsecured debt obligations being rated, in the case of Moody’s, “P-1” and in the case of S&P, “A-1”;

“**Moody’s**” means Moody’s Investors Service, Inc., a Delaware corporation, and any successor thereto and, if such corporation shall for any reason no longer perform the functions of a securities rating agency, Moody’s shall be deemed to refer to any other internationally recognised rating agency designated by the Trustee with the prior written approval of the Issuer;

A “**Negative Rating Event**” shall be deemed to have occurred if (i) the Issuer does not, either prior to or not later than 14 days after the date of a Negative Certification in respect of the relevant Restructuring Event, seek, and thereupon use all reasonable endeavours to obtain, a rating of the Bonds or any other unsecured and unsubordinated debt of the Issuer (or of any Subsidiary of the Issuer which is guaranteed on an unsecured and unsubordinated basis by the Issuer) having an initial maturity of five years or more from a Rating Agency or (ii) if it does so seek and use such endeavours, it is unable, as a result of such Restructuring Event, to obtain such a rating of at least Investment Grade;

“**Non-Appointed Cashflow**” means the actual income of the Issuer in relation to any business (other than the Appointed Business);

“**Non-Appointed Expenses**” means any expense (excluding depreciation and recharge of depreciation by the Appointed Business) incurred in connection with activities other than the Appointed Business, (including for the avoidance of doubt, capital expenditure) as shown in the Financial Statements for the relevant period;

“**Non-Appointed Net Expenditure**” means the Non-Appointed Expenses less the Non-Appointed Cashflow;

“**Official List**” means the official list of the UK Listing Authority;

“**OFWAT**” means the Water Services Regulation Authority, including any successor office or body;

“**Parent**” means South Staffordshire plc;

“**Periodic Review**” means the periodic review of “K” (as defined in the Instrument of Appointment);

“**Permitted Business**” means any Appointed Business and any Permitted Non-Appointed Business;

“**Permitted Encumbrance**” means:

- (a) encumbrances arising under the Loan Finance Documents;
- (b) encumbrances arising by operation of law;
- (c) encumbrances arising in the ordinary course of business and securing amounts not more than 90 days overdue or which are being contested in good faith;
- (d) encumbrances arising from bankers’ liens or from retention of title rights on normal commercial terms in respect of goods supplied, and contractual liens and rights of set off arising in the ordinary course of the business of the Issuer;
- (e) encumbrances approved in writing by the Trustee;
- (f) further secured obligations (including obligations secured by encumbrances arising under Finance Leases) up to an aggregate of 10 per cent. of RAV (other than an encumbrance comprising a netting or set-off arrangement or other encumbrance entered into by a member of the Group arising under any hedging arrangement);
- (g) encumbrances in relation to taxes not yet assessed or, if assessed, not yet due or actively contested in good faith by appropriate proceedings (and for the payment of which adequate reserves have been made, or when required in order to pursue such proceedings an adequate bond has been provided);
- (h) encumbrances arising out of judgments with respect to which at the time (i) an appeal or proceeding for review is actively being prosecuted in good faith and for the payment of which adequate reserves have been made, or where required in order to pursue such proceedings, an adequate bond has been provided; and (ii) a stay of execution shall have been secured (and is still in force) pending such appeal or proceeding for review;

- (i) an encumbrance comprising a netting or set-off arrangement entered into by a member of the Group arising under any hedging arrangement up to an aggregate of 10 per cent. of RAV; or
- (j) rights of set off or bankers' liens or similar such arrangements arising by virtue of the provision of any overdraft facility or any overdraft arising in the ordinary course of business or otherwise as part of an arrangement involving the combination of the Issuer's bank accounts;

**"Permitted Existing Non-Appointed Business"** means any business or businesses other than the Appointed Business which is carried on by the Issuer at the date of this Agreement and (a) the conduct of which falls within the Permitted Non-Appointed Business Limits and (b) in respect of which all material risks related thereto are insured in accordance with Good Industry Practice, and (c) which does not give rise to any material actual or contingent liabilities for the Issuer that are not properly provided for in its Financial Statements;

**"Permitted New Non-Appointed Business"** means any business or businesses other than the Appointed Business and Permitted Existing Non-Appointed Business provided that (a) such business: (i) is prudent in the context of the overall business of the Issuer and continues to be prudent for the duration of that Permitted New Non-Appointed Business; and (ii) is not reasonably likely to be objected to by the DGWS; and (iii) the conduct of which falls within the Permitted Non-Appointed Business Limits; (b) all material risks related thereto are insured in accordance with Good Industry Practice; and (c) such business does not give rise to any material actual or contingent liabilities for the Issuer that are not properly reserved or provided for;

**"Permitted Non-Appointed Business"** means Permitted Existing Non-Appointed Business and Permitted New Non-Appointed Business;

**"Permitted Non-Appointed Business Limits"** means, in respect of the most recently completed Test Period, that the Non-Appointed Net Expenditure did not exceed 5 per cent. of the Appointed Expenses for such Test Period;

**"Potential Event of Default"** means any event which would (with the expiry of any relevant grace period or the giving of notice hereunder or the making of any determination hereunder or any combination thereof) if not remedied or waived become an Event of Default;

**"Presentation Date"** means a day which:

- (i) is or falls after the relevant due date, but, if the due date is not or was not a Business Day in London, is or falls after the next following such Business Day; and
- (ii) is a Business Day in the place of the specified office of the Paying Agent at which the Bond or Coupon is presented for payment and, in the case of payment by transfer to a sterling account with a bank in London as referred to in these Terms and Conditions, in London;

**"Projected Debt Service"** means the aggregate of interest (adjusted for indexation where relevant in accordance with Condition 6 or any other agreement entered into by the Issuer which provides for the payment of interest) due and payable in respect of Indebtedness for Borrowed Money (for the avoidance of doubt, excluding any indexation) during any Calculation Period;

A **"Put Event"** occurs:

- (i) if the Instrument of Appointment is terminated except in respect of such part of its area as is the subject of an appointment or variation by virtue of section 7(4)(b) or (bb) of the Act; or
- (ii) in the case of the occurrence of a Restructuring Event, on the date of the last to occur of (aa) such Restructuring Event, (bb) either a Rating Downgrade or, as the case may be, a Negative Rating Event and (cc) the relevant Negative Certification;

**"Qualifying Bank"** means any bank which is authorised to accept deposits (for the purposes of the Financial Services and Markets Act 2000) and whose short term debt is rated at least "A-1" by S&P and "P-1" by Moody's and whose long-term debt is at least "AA"- by S&P and at least "Aa3" by Moody's, or in the case of a bank whose long-term debt is not rated, a bank of equivalent standing

approved by the Trustee or any bank specifically approved in writing by the Trustee, provided that such bank has its short term debt rated at least “A-1” by S&P and “P-1” by Moody’s;

“**Rated Securities**” means the Bonds, if at any time and for so long as they have a rating from a Rating Agency, and otherwise any other unsecured and unsubordinated debt of the Issuer (or of any Subsidiary of the Issuer which, in any such case, is guaranteed on an unsecured and unsubordinated basis by the Issuer) having an initial maturity of five years or more which is rated by a Rating Agency;

“**Rating Agencies**” means S&P and Moody’s, or their respective successors and “**Rating Agency**” means any one of them;

A “**Rating Downgrade**” shall be deemed to have occurred in respect of a Restructuring Event if the then current rating assigned to the Rated Securities by any Rating Agency (whether provided by a Rating Agency at the invitation of the Issuer or by its own volition) is withdrawn or reduced from an Investment Grade rating to a non-investment grade rating (BB+/Ba1, or their respective equivalents for the time being, or worse) or, if the Rating Agency shall then have already rated the Rated Securities below Investment Grade, the rating is lowered one full rating category (from BB+/Ba1 to BB/Ba2 or such similar lowering);

“**Regulated Asset Ratio**” or “**RAR**” means, in relation to a Calculation Date, the ratio of:

- (a) Total Net Indebtedness; to
- (b) Regulated Asset Value,

on the current Calculation Date or immediately preceding each Calculation Date falling on 31 March of each year and as forecast for any subsequent Calculation Dates falling on 31 March up to and including the Final Forecast Date or in such other period expressly stated in each case, based on the best information available and provided that, where a draft OFWAT determination is available prior to the publication of a final OFWAT determination, the figures set out in such draft OFWAT determination shall be used, unless otherwise agreed by the Trustee;

“**Regulated Asset Value**” or “**RAV**” means the regulatory asset base of the Issuer most recently published by OFWAT for the applicable Financial Year end, adjusted for inflation to the most recent Calculation Date falling on 31 March, based on the best available information and provided that where a draft OFWAT determination is available, the figures set out in such draft OFWAT determination shall be used, adjusted for inflation, unless otherwise agreed by the Trustee;

“**Relevant Payments**” means (i) any payment to any Affiliate of the Issuer made by or on behalf of the Issuer by way of dividend, loan (or repayment of any loan), redemption, purchase, discharge by way of set-off, counterclaim, other distribution of any sort, or otherwise, whether in cash or in kind, and whether pursuant to the terms of any agreement or otherwise or by way of gift (other than a payment pursuant to an arrangement permitted by Condition 4(d)(iii)) and (ii) the payment of any rebate to customers of the Issuer generally, or any category of them, made by or on behalf of the Issuer (excluding compensation payments and refunds to customers in accordance with Good Industry Practice);

“**Restructuring Event**” means the occurrence of one or both of the following events:

- (a) any material rights, benefits or obligations of the Issuer as a water undertaker or sewerage undertaker arising under the Instrument of Appointment or the Act as in force on the Closing Date or any material terms of the Instrument of Appointment are modified (whether or not with the consent of the Issuer and whether pursuant to the Water Industry Act or otherwise) unless two directors of the Issuer have certified to the Trustee that such modified rights, benefits, obligations or terms are not materially less favourable to the business of the Group and to the business of the Issuer (provided that an adjustment to K shall not fall within this paragraph (a)); or
- (b) any legislation (whether primary or subordinate) is enacted removing, reducing or qualifying the duties or powers of the Secretary of State for the Environment (or any successor) and/or the Director General of Water Services (or any successor) (including any such legislation removing, reducing or qualifying such duties or powers under or pursuant to sections 2, 9 or 24 of the Act but excluding, in all circumstances, the Water Act 2003) in each case as compared to those in

force on the Closing Date unless two directors of the Issuer have certified in good faith to the Trustee that such removal, reduction or qualification is unlikely to have a material adverse effect on the financial condition of the Group and the Issuer;

**“Restructuring Period”** means:

- (a) if at any time a Restructuring Event occurs there are Rated Securities, the period of 60 days starting from and including the day on which that Restructuring Event occurs; or
- (b) if at the time a Restructuring Event occurs there are no Rated Securities, the period starting from and including the day on which that Restructuring Event occurs and ending on the day 60 days following the later of (aa) the date on which the Issuer shall seek to obtain a rating as contemplated in the definition of Negative Rating Event prior to the expiry of the 14 days referred to in that definition and (bb) the date on which a Negative Certification shall have been given to the Issuer and the Trustee in respect of that Restructuring Event;

**“S&P”** means Standard & Poor’s Ratings Services and any successor thereto and, if such corporation shall for any reason no longer perform the functions of a securities rating agency, S&P shall be deemed to refer to any other internationally recognised rating agency designated by the Trustee with the prior written approval of the Issuer;

**“Subsidiary”** means a subsidiary within the meaning of section 736 of the Companies Act 1985 and, for the purpose of Condition 4(b) and in relation to financial statements of the Group, a subsidiary undertaking within the meaning of section 258 of the Companies Act 1985;

**“Tax”** means any tax, levy, impost, duty or other charge or withholding of a similar nature (including any penalty or interest payable in connection with any failure to pay or any delay in paying any of the same);

**“Test Period”** means each period of 36 months ending on 31 March in each year;

**“Third Party Guarantee”** means any guarantee, indemnity or other assurance against financial loss (whether actual or contingent, future or present) given in respect of the Indebtedness for Borrowed Money of another person; and

**“Total Net Indebtedness”** means as at the relevant date, any Indebtedness for Borrowed Money of the Issuer less Cash and Cash Equivalents.

Any reference to an obligation being guaranteed shall include a reference to an indemnity being given in respect of the obligation.

## **21. Governing Law**

The Trust Deed, these Terms and Conditions, the Bonds and the Coupons are governed by, and will be construed in accordance with, English law.

## **22. Contracts (Rights of Third Parties) Act 1999**

No rights are conferred on any person under the Contracts (Rights of Third Parties) Act 1999 to enforce any term of the Bonds or the Coupons but this does not affect any right or remedy of any person which exists or is available apart from that Act.

## USE OF PROCEEDS

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The net proceeds of the issue of the Bonds, expected to amount to approximately £34,825,000.00 will be used by the Issuer for lending to an intermediate parent company of the Issuer for refinancing existing indebtedness and for general corporate purposes.



## SUMMARY OF PROVISIONS RELATING TO THE BONDS WHILE IN GLOBAL FORM

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The Global Bonds contain provisions which apply to the Bonds while they are in global form, some of which modify the effect of the Terms and Conditions of the Bonds set out in this document. The following is a summary of certain of those provisions.

### 1. Exchange

The Temporary Global Bond is exchangeable in whole or in part (free of charge to the holder) for interests in the Permanent Global Bond on or after a date which is expected to be 11 August 2008 upon certification as to non-U.S. beneficial ownership in the form set out in the Trust Deed. The Permanent Global Bond is exchangeable in whole but not in part (free of charge to the holder) for the definitive Bonds described below (a) if the Permanent Global Bond is held on behalf of a clearing system and such clearing system is closed for business for a continuous period of 14 days (other than by reason of holidays, statutory or otherwise) or announces an intention permanently to cease business or does in fact do so and no alternative clearing system satisfactory to the Trustee is available, or (b) if the Issuer would suffer a material disadvantage in respect of the Bonds as a result of a change in the laws or regulations (taxation or otherwise) of the United Kingdom which would not be suffered were the Bonds in definitive form and a certificate to such effect signed by two directors of the Issuer is delivered to the Trustee. Thereupon (in the case of (a) above) the holder of the Permanent Global Bond (acting on the instructions of a person having a beneficial interest in the Permanent Global Bond) or the Trustee may give notice to the Issuer, and (in the case of (b) above) the Issuer may give notice to the Trustee and the Bondholders, of its intention to exchange the Permanent Global Bond for definitive Bonds on or after the Exchange Date (as defined below).

On or after the Exchange Date the holder of the Permanent Global Bond may surrender the Permanent Global Bond to or to the order of the Principal Paying Agent. In exchange for the Permanent Global Bond, the Issuer will deliver, or procure the delivery of, an equal aggregate principal amount of duly executed and authenticated definitive Bonds (having attached to them all Coupons in respect of interest which has not already been paid on the Permanent Global Bond and in respect of which claims shall not have become prescribed), security printed in accordance with any applicable legal and stock exchange requirements and in or substantially in the form set out in the Trust Deed. On exchange of the Permanent Global Bond, the Issuer will, if the holder so requests, procure that it is cancelled and returned to the holder together with any relevant definitive Bonds.

“Exchange Date” means a day specified in the notice requiring exchange falling not less than 60 days after that on which the notice requiring exchange is given and on which banks are open for general business in the place in which the specified office of the Principal Paying Agent is located and, except in the case of exchange pursuant to (a) above, in the place in which the relevant clearing systems are located.

### 2. Payments

No payment will be made on the Temporary Global Bond unless, on or after 11 August 2008, exchange for an interest in the Permanent Global Bond is improperly withheld or refused. Payments of principal and interest in respect of Bonds represented by the Permanent Global Bond will, subject as set out below, be made against presentation for endorsement and, if no further payment falls to be made in respect of the Bonds, surrender of the Permanent Global Bond to or to the order of the Principal Paying Agent or such other Paying Agent as shall have been notified to the Bondholders for such purpose. A record of each payment so made will be endorsed on the appropriate schedule to the Permanent Global Bond, which endorsement will be *prima facie* evidence that such payment has been made in respect of the Bonds. Payments of interest on the Temporary Global Bond (if permitted by the first sentence of this paragraph) will be made only upon certification as to non-U.S. beneficial ownership, unless such certification has already been made.

### 3. Notices

So long as the Bonds are represented by one or both of the Global Bonds and such Global Bond(s) is/are held on behalf of a clearing system, notices to Bondholders may be given by delivery of the relevant

notice to that clearing system for communication by it to entitled accountholders in substitution for publication as required by Condition 16 provided that, so long as the Bonds are admitted to listing by the UK Listing Authority and admitted to trading on the London Stock Exchange, the requirements of the UK Listing Authority have been complied with. Any such notice shall be deemed to have been given to the Bondholders on the day on which such notice is delivered to the clearing system(s) as aforesaid.

#### **4. Prescription**

Claims against the Issuer in respect of principal and interest on the Bonds while the Bonds are represented by a Global Bond shall be prescribed and become void unless it is presented for payment within a period of 10 years (in the case of principal) and five years (in the case of interest) from the appropriate Relevant Date (as defined in Condition 10).

#### **5. Cancellation**

Cancellation of any Bond represented by a Global Bond and required by the Terms and Conditions to be cancelled following its redemption or purchase will be effected by endorsement by or on behalf of the Principal Paying Agent of the reduction in the principal amount of such Global Bond on the relevant part of the Schedule thereto.

#### **6. Trustee's Powers**

While the Bonds are represented by one or both of the Global Bonds and such Global Bond(s) is/are held on behalf of a clearing system, the Trustee may, in considering the interests of Bondholders, have regard to any information provided to it by such clearing system or its operator as to the identity (either individually or by category) of its accountholders with entitlements to the Global Bond(s) and may consider such interests as if such accountholders were the holder(s) of the Global Bond(s).

#### **7. Put Option**

For so long as all of the Bonds are represented by one or both of the Global Bonds and such Global Bond(s) is/are held on behalf of a clearing system, the option of the Bondholders provided for in Condition 9 may be exercised by the holder of the relevant Global Bond giving either a duly completed Put Notice or a duly completed notice of exercise in accordance with the standard procedures of the relevant clearing system to the Principal Paying Agent of the principal amount of the Bonds in respect of which such option is exercised and at the same time presenting or procuring the presentation of the relevant Global Bond to the Principal Paying Agent for notation accordingly within the time limits set forth in that Condition.

#### **8. Call Option**

For so long as all of the Bonds are represented by one or both of the Global Bonds and such Global Bond(s) is/are held on behalf of a clearing system, no drawing of Bonds will be required under Condition 8(c) in the event that the Issuer exercises its call option in Condition 8(c) in respect of less than the aggregate principal amount of Bonds outstanding. In such event, the standard procedures of the relevant clearing system shall operate to determine which interests in the Global Bond(s) are to be subject to such option.

#### **9. Denominations**

The Bonds are issued in the denomination of £50,000.

## SOUTH STAFFORDSHIRE WATER PLC

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### Overview

South Staffordshire Water plc (“SSW”) is a licensed water undertaker operating in the UK within the regulatory framework established under the Water Industry Act 1991, as amended, on 25 November 1991. It supplies clean water only (i.e. not sewerage services) to a population of nearly 1.25 million in both urban and rural areas covering 1,500 square km in the Midlands, UK. SSW is the third largest Water Only Company (“WOC”) in the UK in terms of population supplied. Turnover of SSW for the year ended 31 March 2007 amounted to £76.7 million.

Of the 22 water companies in England and Wales, SSW has the third lowest average annual household bill (approximately 24 per cent. below the industry average) for 2007-2008, the fifth highest levels of service for the year to 31 March 2007\*, as measured by the Office of Water Services (“Ofwat”) in its overall performance assessment, and its operating cost base is one of the most efficient, ranked in the highest category for 2006/07 by Ofwat. SSW has an experienced management team with significant water sector experience.

SSW is a wholly owned subsidiary of South Staffordshire Plc (“SS Plc”). In addition to SSW, SS Plc comprises three closely related non-regulated businesses which provide customer service and billing, water and sewer infrastructure maintenance and bottled spring water. SSW is not financially or operationally dependent on any entities within the group of companies comprising SS Plc and its subsidiaries (the “Group”), although SSW contracts with other members of the Group for the provision of services for open market value or at cost.

The business address of SSW is Green Lane, Walsall, WS2 7PD and the telephone number is 01922 638282.

### Regulation

- Regulatory framework

The economic activities of the regulated water companies in the UK including SSW are regulated pursuant to the Water Industry Act 1991, as amended, and the conditions of their respective instruments of appointment.

Ofwat is the economic regulator for the water and sewerage industry in England and Wales. In addition, water companies are also subject to regulations by the Environment Agency and the DWI.

A key responsibility of Ofwat is the determination of water charges. The current review period is the fourth since the privatisation of the industry. As part of this review process, Ofwat also sets expected levels of capital investment, minimum service levels and other specific outputs for delivery in the period.

Ofwat has a statutory duty to exercise and perform its powers and duties conferred or imposed under the Water Industry Act 1991, as amended, in a manner it considers best calculated to ensure that:

- the functions of regulated water companies are properly carried out throughout England and Wales; and
- regulated water companies are able (in particular, by securing reasonable returns on their capital) to finance the proper execution of their functions.

SSW has a duty to develop and maintain an efficient and economical system of water supply in its licensed area. Also, it has duties to supply water for domestic purposes to premises within the areas set out in the Licence (as defined below) and which are connected to a water main and to connect new premises to a water main. It has no responsibilities for sewerage or drainage services within its supply area, these being the duties of Severn Trent Water Ltd.

Ofwat regulates water charges by capping the revenue which a company can charge by setting the average decrease or increase in charges which a company can impose in any year, taking into account the impact of inflation.

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\* Extracted from information supplied by Ofwat.

Ofwat seeks to enable well managed companies to finance the delivery of their services in line with relevant standards and requirements and to provide incentives for companies to improve efficiency and service delivery.

- Regulatory determination for 2005 to 2010

In December 2004 Ofwat set prices for the five years from 2005 to 2010, having considered the business plans submitted by the water companies in April 2004. The price limits for the five-year period set for SSW correspond to an aggregate 16.4 per cent. increase in real terms over the period, being an annual average increase of 3.2 per cent.

Limits on annual price increases for SSW are as follows\*:

2005/06	2006/07	2007/08	2008/09	2009/10
+9.9%	+2.5%	+1.7%	+1.0%	+1.3%

The average domestic water bill for SSW is expected to rise by £15 over the five years (excluding inflation) compared to an average increase of £23 for the industry as a whole.

- Strategy

A key feature of the Periodic Review (as defined in Condition 20) is the production of SSW's strategic business plan. This plan confirmed that SSW's strategy for the five years to 2010 would be as follows:

- Increase levels of mains renewal (replacement) by around 40 per cent.;
- Maintain leakage levels;
- Increase the effectiveness of maintenance expenditure;
- Consolidate position of leading efficiency, pursuing new initiatives and taking account of the benefits of technology advances;
- Continue to provide high levels of customer service; and
- Ensure a reliable and continuous supply of water to all its customers.

The price determination has provided certainty for the five years to 2010 and allows SSW to invest to maintain existing high quality and service standards, while keeping charges to its customers amongst the lowest in the industry.

- The Licence

The Licence was originally granted to SSW in August 1989. It specifies the geographical areas served and imposes conditions on SSW, which include limits on charges to customers and restrictions on the financial activities of SSW.

Under the Water Industry Act 1991, as amended, the conditions of the Licence may be modified by Ofwat either (i) with the consent of SSW, or (ii) without SSW's consent following a reference to the Competition Commission, which concludes that there are effects adverse to the public interest, which can be remedied or prevented by modifications.

### ***Termination of the Licence***

Under the Water Industry Act 1991, as amended, and the conditions of the Licence, there are only certain circumstances in which SSW could cease to hold its Licence for all or part of its licensed area, and these are if:

- SSW consented to such a change;
- the Secretary of State has given 25 years' notice to terminate;

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\* Extracted from information supplied by Ofwat.

- SSW is in special administration, and the “special administrator” (as defined under the Water Industry Act 1991) opts to transfer the business and Licence to a successor; or
- an inset appointment is granted over part of SSW’s area to another company, whereby an industrial customer using more than 50 million litres of water per annum, opts to use a different supplier and reaches agreement with Ofwat to amend the Licence.

As at the date of this Prospectus, no compulsory licence terminations or special administration orders have been made in connection with any appointed activities of any regulated company in England and Wales.

## History

The South Staffordshire Waterworks Company, a statutory water company, was formed in 1853 to provide an abundant supply of pure water to the inhabitants of the towns of the Black Country in the UK. South Staffordshire Waterworks Company became a public limited company in 1991 and was listed on the London Stock Exchange as South Staffordshire Water plc. In February 1992 a capital reorganisation took place involving a share for share transfer which resulted in South Staffordshire Water Holdings Limited becoming the listed entity, being the ultimate parent of the wholly-owned SSW. This was the first step in the creation of non-regulated businesses. In recognition of the success of those non-regulated businesses, South Staffordshire Water Holdings was renamed South Staffordshire Group Plc in 1999 and was reclassified to the FTSE Support Services sector in 2001.

In April 2004, South Staffordshire Group Plc was renamed Homeserve, and SS Plc, comprising SSW and its closely related non-regulated businesses, was demerged as a separately listed company on the London Stock Exchange.

In November 2004, SS Plc was acquired by AqualInvest Acquisitions Limited, a company beneficially controlled by Arcapita Bank B.S.C.(C). SS Plc was delisted in December 2004.

In October 2007, SS Plc was acquired by Alinda Infrastructure Fund, an independent institutional investor in infrastructure assets.

## Area of supply

SSW is a licensed water undertaker operating within the regulatory framework established under the Water Industry Act 1991, as amended. SSW’s principal activities comprise the supply of clean water in the West Midlands. SSW’s area of supply is completely surrounded by the neighbouring Severn Trent Water Ltd, which also provides sewerage services within SSW’s area. SSW supplies water to a population of nearly 1.25 million, in an area which covers 1,490 square km. It has a diverse catchment area in the Midlands covering both urban and rural areas, spreading from Uttoxeter and the Peak District in the North to the outskirts of Stourbridge in the South and from Dudley in the West to Sutton Coldfield, Tamworth and Burton in the East, reaching the outskirts of Derby at the Toyota Motor Company works at Findern. SSW is the sole supplier of drinking water in the area it serves.

## Customer base

SSW serves both residential households and commercial and industrial customers. SSW has approximately 509,000 connected household properties, of which approximately 403,000 are charged annually on an unmeasured basis based upon the rateable value of the property (rather than on the volume of water consumed). The remaining approximately 106,000 properties, being approximately 21 per cent. of the domestic property base, are charged on a metered basis reflecting the volume of water used. All new properties are required to be fitted with a meter and customers can opt to have a meter installed at the Company’s expense. In the past three years 5,000 customers on average per annum, being one per cent. of the domestic property base, have opted to have a meter installed.

SSW has a lower meter penetration than the industry average of 33 per cent., reflecting the low level of charges and the healthy water resource position of SSW.

SSW also has 36,000 commercial and industrial customers from a wide range of sectors. No one customer accounts for more than one per cent. of turnover and the company's 10 largest water users account for approximately 3.5 per cent. of turnover. SSW therefore has a diversified customer base with no large single customer dependency.

### **Water resources and demand**

SSW has a wide variety of water resources available and its resource position is stable. Water can be drawn from the impounding reservoir at Blithfield, from the River Severn and from deep boreholes, and consequently SSW has avoided hosepipe bans for over 30 years. Approximately 40 per cent. of water is supplied from the Hampton Loade Treatment Works on the River Severn near Bridgnorth, Shropshire. SSW's second largest treatment works at Seedy Mill, near Lichfield, accounts for 20 per cent. of water supplied and treats water from Blithfield Reservoir. SSW also has twenty four boreholes supplying 40 per cent. of the water it supplies to consumers.

On average SSW supplies 330 million litres per day (ML/d) every day of the year, with demand rising in the summer to a peak in 2006/07 of 420 ML/d. SSW has capacity to supply up to 440 ML/d of water on average throughout the year, which increases to meet peak demand, including the use of reservoir storage. No material water supply or resource difficulties have been experienced which have resulted in restrictions on usage of water by its customers (including the imposition of hosepipe bans) for the last 30 years.

In order to treat the water and distribute it to its customers, SSW had at 31 March 2007:

- 5,895 km of water mains
- 47 water pumping booster stations
- 24 wells and boreholes
- 3 river abstractions
- 26 water treatment works

As part of the 2004 Periodic Review, Ofwat set a leakage target for SSW of 75 ML/d. This target has been achieved in each of the first two years of the current five year review period.

### **Customer service tariffs and billing\***

SSW continues to provide high levels of service to its customers. SSW was placed in fifth position across the water industry for 2006/07 (the last year for which results have been published), based on Ofwat's overall performance assessment which measures performance on levels of customer service, leakage, water quality and supply resilience with a score of 283 points out of 288. This confirmed a top five place for SSW in each of the last eight years.

For 2007/08, the domestic customers of SSW have the third lowest water charge in England and Wales, with an annual average household bill of £113 (25 per cent. below the national average as reported by Ofwat). SSW's customers who use more than 50 million litres per annum can benefit from an industrial tariff which provides a discount compared to domestic tariffs, reflecting the lower costs of supplying these customers.

### **Ofwat efficiency reports\***

The Ofwat report on efficiency in the water industry published in December 2007 ranked SSW in the highest band for both operating costs and capital maintenance expenditure, one of only five companies in the industry to achieve this.

SSW has been ranked by Ofwat in the highest band for operating costs for each of the past five years. This reflects continued efficiency initiatives over the period including a reduction in headcount, closure of

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\* Extracted from information supplied by Ofwat.

area offices, outsourcing of some services (in some cases to associated companies) and the greater use of technology and automation.

### Water quality requirements

Stringent water quality standards are set for the supply of water by the EU. For the year ended 31 December 2006 (the latest year for which results have been published) SSW achieved 99.97 per cent. compliance, as reported by the DWI.

### Capital expenditure plans

The Periodic Review of prices in 2004 provided for capital expenditure of £92 million by SSW (at 2002/3 prices) net of contributions, equivalent to £111 million at outturn prices.

Capital expenditure for the two years to 31 March 2007 is a cumulative spend of £42 million, £2 million less than the first two years of the Final Determination. It is anticipated that this will be brought in line with the determination during 2007/08. It is also expected that expenditure over the five-year review period as a whole will be in line with the Final Determination.

### Employees

The number of employees of SSW as at 31 March 2007 is 380.

### Directors

As at the date of this Prospectus, there are eight directors of SSW. Their names, function within SSW and principal outside activities are described below. The business address of the directors of SSW is Green Lane, Walsall, United Kingdom.

<i>Name of Director</i>	<i>Position</i>	<i>Years with SSW</i>	<i>Principal outside activities</i>
Jack Carnell	Managing Director	33	Director of SS Plc, National President of the Institute of Water Officers and Chairman of USIT, the Water Industry Charity for Training and the “Regulated industries” representative on the Environment Agency’s Strategy Forum
Adrian Page	Finance Director	12	Group Finance Director, SS Plc, Director of Echo Managed Services, Onsite Central, Integrated Water Services, Underground Pipeline Services, Hydrosave, Perco Engineering Services, Portadam, Office Water Coolers
Liz Swarbrick	Asset Management Director	19	
Keith Marshall	Supply and Resources Director	34	Director of Integrated Water Services
David Sankey	Non-Executive Chairman	25	Executive Chairman, SS Plc, Director of Onsite Central, Echo Managed Services
Panton Corbett	Non-Executive	15	Non-executive Director of SS Plc and Haynes Publishing Group PLC
Mike Hughes	Non-Executive	4	Non-executive Director of SS Plc, Director of EA Technology Ltd and Electricity North West Ltd
Simon Riggall	Non-Executive	0	Non-executive Director of SS Plc, Partner, Alinda Capital Partners

In accordance with the terms of the Licence, SSW is required to have three independent non-executive directors. These are David Sankey, Panton Corbett and Mike Hughes. Simon Rigall is not considered to be an independent non-executive director.

As at the date of this Prospectus, no director has any or potential conflict of interest between his or her duties to SSW and his or her private interests or other duties.



## UNITED KINGDOM TAXATION

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The following is of a general nature and applies only to persons who are the beneficial owners of Bonds and is a summary of the Issuer's understanding of current law and practice in the United Kingdom as at the date of this Prospectus relating to certain aspects of United Kingdom taxation. The summary is non-exhaustive. It does not necessarily apply where the income is deemed for tax purposes to be the income of any other person. Some aspects do not apply to certain classes of person (such as dealers, collective investment schemes and persons connected with the Issuer) to whom special rules may apply. Prospective Bondholders or Couponholders who may be subject to tax in a jurisdiction other than the United Kingdom or who may be unsure as to their tax position should seek their own professional advice.

### A. Interest on the Bonds

#### 1. *Payment of interest on the Bonds*

Payments of interest on the Bonds may be made without deduction of or withholding on account of United Kingdom income tax provided that the Bonds continue to be listed on a "recognised stock exchange" within the meaning of section 1005 of the Income Tax Act 2007 (the "Act"). The London Stock Exchange is a recognised stock exchange. Securities will be treated as listed on the London Stock Exchange if they are included in the Official List (within the meaning of and in accordance with the provisions of Part 6 of the Financial Services and Markets Act 2000) and admitted to trading on the London Stock Exchange. Accordingly, provided that the Bonds remain so listed, interest on the Bonds will be payable without withholding or deduction on account of United Kingdom income tax.

Interest on the Bonds may also be paid without withholding or deduction on account of United Kingdom income tax where interest on the Bonds is paid by a company and, at the time the payment is made, the Issuer reasonably believes (and any person by or through whom interest on the Bonds is paid reasonably believes) that the beneficial owner of such interest is within the charge to United Kingdom corporation tax as regards the payment of interest, provided that HM Revenue & Customs ("HMRC") has not given a direction (in circumstances where it has reasonable grounds to believe that it is likely that the above exemption is not available in respect of such payment of interest at the time the payment is made) that the interest should be paid under deduction of tax.

In other cases, an amount must generally be withheld from payments of interest on the Bonds on account of United Kingdom income tax at the savings rate (currently 20 per cent.) (or, if the Finance Bill 2008 is enacted in its current form, from 6 April 2008 the basic rate, which would also be 20 per cent). However, where an applicable double tax treaty provides for a lower rate of withholding tax (or for no tax to be withheld) in relation to a Bondholder, subject to satisfaction of certain procedural requirements, HMRC can issue a notice to the Issuer to pay interest to the Bondholder without deduction of tax (or for interest to be paid with tax deducted at the rate provided for in the relevant double tax treaty).

Bondholders who are individuals may wish to note that, in certain circumstances, HMRC has power to obtain information (including the name and address of the beneficial owner of the interest and the amount of interest paid or received) from any person in the United Kingdom who either pays or credits interest to or receives interest for the benefit of a Bondholder, or who either pays amounts payable on the redemption of Bonds to or receives such amounts for the benefit of another person. Information so obtained may, in certain circumstances, be provided by HMRC to the tax authorities of the jurisdiction in which the Bondholder is resident for tax purposes.

#### 2. *EC Savings Directive*

Under the Savings Directive, Member States are required to provide to the tax authorities of another Member State details of payments of interest (or similar income) paid by a person within its jurisdiction to an individual or to certain non-corporate entities resident in that other Member State (or of certain payments secured for their benefit). However, for a "transitional period", Belgium, Luxembourg and Austria are instead required (unless during that period they elect otherwise) to operate a withholding system in relation to such payments (the ending of such transitional period being dependent upon the conclusion of certain other agreements relating to information exchange with certain other countries). A

number of non-EU countries and territories including Switzerland have adopted similar measures (a withholding system in the case of Switzerland).

### 3. *Further United Kingdom Income Tax Issues*

Interest on the Bonds constitutes United Kingdom source income for tax purposes and, as such, may be subject to income tax by direct assessment even where paid without withholding.

However, interest with a United Kingdom source received without deduction or withholding on account of United Kingdom tax will not be chargeable to United Kingdom tax in the hands of a Bondholder (other than certain trustees) who is not resident for tax purposes in the United Kingdom unless that Bondholder carries on a trade, profession or vocation in the United Kingdom through a United Kingdom branch or agency in connection with which the interest is received or to which the Bonds are attributable (or where that Bondholder is a company, unless that Bondholder carries on a trade in the United Kingdom through a permanent establishment in connection with which the interest is received or to which the Bonds are attributable). There are exemptions for interest received by certain categories of agent (such as some brokers and investment managers). The provisions of an applicable double taxation treaty may also be relevant for such Bondholders.

## **B. United Kingdom Corporation Tax Payers**

In general, Bondholders which are within the charge to United Kingdom corporation tax will be charged to tax on income in respect of all returns, profits or gains on, and fluctuations in value of, the Bonds (whether attributable to interest, currency fluctuations or otherwise) broadly in accordance with generally accepted accounting practice.

## **C. Other United Kingdom Tax Payers**

### 1. *Taxation of Chargeable Gains*

The Bonds will constitute “qualifying corporate bonds” within the meaning of section 117 of the Taxation of Chargeable Gains Act 1992. Accordingly, a disposal by a Bondholder of a Bond will not give rise to a chargeable gain or an allowable loss for the purposes of the UK taxation of chargeable gains.

### 2. *Taxation of Discount*

Notwithstanding paragraph 1 above, the Bonds will constitute “deeply discounted securities” for the purposes of Chapter 8 of Part 4 of the Income Tax (Trading and Other Income) Act 2005. Therefore, any gain realised on redemption or transfer of the Bonds will generally be taxable as income but such Bondholder will not be able to claim relief from income tax in respect of costs incurred on the acquisition, transfer or redemption, or losses incurred on the transfer or redemption, of the Bonds.

## **D. Stamp Duty and Stamp Duty Reserve Tax (SDRT)**

No United Kingdom stamp duty or SDRT is payable on the issue or a transfer by delivery of the Bonds.

## SUBSCRIPTION AND SALE

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Barclays Bank PLC (the “**Manager**”) has, pursuant to a Subscription Agreement dated 26 June 2008 (the “**Subscription Agreement**”), agreed with the Issuer, subject to the satisfaction of certain conditions, to subscribe for the Bonds at the issue price of 100 per cent. of their principal amount. The Manager is entitled to terminate the Subscription Agreement in certain circumstances prior to payment to the Issuer. The Issuer has agreed to indemnify the Manager against certain liabilities in connection with the issue of the Bonds. The address of the Manager is 5 The North Colonnade, Canary Wharf, London E14 4BB.

The Bonds have not been and will not be registered under the Securities Act and may not be offered, sold or delivered within the United States or to, or for the account or benefit of, U.S. persons except in accordance with Regulation S under the Securities Act or pursuant to an exemption from the registration requirements of the Securities Act. The Bonds have not been approved or disapproved by the U.S. Securities and Exchange Commission, any state securities commission in the United States or any other U.S. regulatory authority, nor have any of the foregoing authorities passed upon or endorsed the merits of offering the Bonds or the accuracy or adequacy of this Prospectus.

The Bonds are subject to U.S. tax law requirements and may not be offered, sold or delivered within the United States or its possessions or to a United States person, except in certain transactions permitted by U.S. tax regulations. Terms used in this paragraph have the meanings given to them by the U.S. Internal Revenue Code of 1986 and regulations thereunder.

The Manager has agreed that, except as permitted by the Subscription Agreement, it will not offer, sell or deliver the Bonds: (a) as part of their distribution at any time; or (b) otherwise until 40 days after the later of the commencement of the offering and the Closing Date within the United States or to, or for the account or benefit of, U.S. persons, and it will have sent to each dealer to which it sells any Bonds during the distribution compliance period a confirmation or other notice setting forth the restrictions on offers and sales of the Bonds within the United States or to, or for the account or benefit of, U.S. persons. Terms used in this paragraph have the meanings given to them by Regulation S under the Securities Act.

In addition, until 40 days after the commencement of the offering, an offer or sale of Bonds within the United States by a dealer that is not participating in the offering may violate the registration requirements of the Securities Act.

The Manager has represented and agreed that: (a) it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to the Bonds in, from or otherwise involving the United Kingdom; and (b) it has only communicated or caused to be communicated and will only communicate or cause to be communicated an invitation or inducement to engage in investment activity (within the meaning of section 21 of the FSMA) received by it in connection with the issue of the Bonds in circumstances in which section 21(1) of the FSMA does not apply to the Issuer.

## GENERAL INFORMATION

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### **Listing**

The admission of the Bonds to the Official List will be expressed as a percentage of their principal amount, exclusive of accrued interest. It is expected that official listing on the London Stock Exchange will be granted on or about the Closing Date, subject only to the issue of the Temporary Global Bond. Prior to official listing and admission to trading, however, dealings in the Bonds will be permitted by the London Stock Exchange in accordance with its rules.

The total expenses related to admission to trading are estimated to amount to approximately £8,600.

### **Legend**

Bonds and Coupons will bear the following legend: "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."

### **Clearing systems**

The Bonds have been accepted for clearance through Euroclear and Clearstream, Luxembourg which are the entities in charge of keeping the records. The Common Code for the Bonds is 037201090 and the ISIN is XS0372010909.

The address of Euroclear is Euroclear Bank SA/NV, 1 Boulevard du Roi Albert II, B-1210 Brussels and the address of Clearstream, Luxembourg is Clearstream Banking, 42 Avenue JF Kennedy, L-1855 Luxembourg.

### **Approvals and Authorisations**

The Issuer has obtained all necessary consents, approvals and authorisations in the United Kingdom in connection with the issue and performance of the Bonds.

The issue of the Bonds was authorised by a resolution of the board of directors of the Issuer passed on 23 May 2008 appointing an executive committee and a resolution of such executive committee passed on 23 June 2008.

### **No significant or material change**

There has been no significant change in the financial or trading position of the Issuer or the Group and no material adverse change in the prospects of the Issuer or the Group since 31 March 2007.

### **Litigation**

The Issuer is not or has not been involved in any governmental, legal or arbitration proceedings, including any such proceedings which are pending or threatened of which the Issuer is aware, in the 12 months preceding the date of this document which may have, or have in such period, a significant effect on the financial position or profitability of the Issuer or the Group.

### **Auditors**

The auditors of the Issuer are Deloitte & Touche LLP, Registered Auditor, who have audited the Issuer's accounts, without qualification, in accordance with generally accepted auditing standards in the United Kingdom for the financial years ended on 31 March 2006 and 31 March 2007.

### **Documents available for Inspection**

Copies of the following documents may be inspected during usual business hours on any weekday (Saturdays, Sundays and public holidays excepted) at the offices of the Issuer at Green Lane, Walsall WS2 7PD during the period of 12 months from the date of this Prospectus:

- (a) the Memorandum and Articles of Association of the Issuer; and

- (b) the audited annual report and accounts of the Issuer for the financial years ended 31 March 2007 and 31 March 2006.

In addition, this Prospectus is also available on the website of the Regulatory News Service operated by the London Stock Exchange at [www.londonstockexchange.com/en-gb/pricesnews/marketnews](http://www.londonstockexchange.com/en-gb/pricesnews/marketnews).

### **Post-issuance Information**

The Issuer does not intend to provide post-issuance information in connection with this issue.

### **Manager transacting with the Issuer**

The Manager and its affiliates have engaged, and may in the future engage, in investment banking and/or commercial banking transactions with, and may perform services to the Issuer and its affiliates in the ordinary course of business.

Save for any fees payable to the Manager, so far as the Issuer is aware, no person involved in the issue of the Bonds has an interest material to the offer.

**REGISTERED OFFICE OF THE ISSUER**

**South Staffordshire Water plc**  
Green Lane  
Walsall  
WS2 7PD

**AUDITORS**

**Deloitte & Touche LLP**  
Four Brindleyplace  
Birmingham  
B1 2HZ

**MANAGER**

**Barclays Bank PLC**  
5 The North Colonnade  
Canary Wharf  
London E14 4BB

**TRUSTEE**

**Citicorp Trustee Company Limited**  
Citigroup Centre  
Canada Square  
Canary Wharf  
London E14 5LB

**PRINCIPAL PAYING AGENT**

**Citibank, N.A., London Branch**  
Citigroup Centre  
Canada Square  
Canary Wharf  
London E14 5LB

**LEGAL ADVISERS**

*To the Manager and the Trustee:*

**Allen & Overy LLP**  
One Bishops Square  
London E1 6AD

*To the Issuer*

**Ashurst LLP**  
5 Appold Street  
London EC2A 2HA

