13 October 2006

SOUTHERN WATER SERVICES (FINANCE) LIMITED

(incorporated with limited liability in the Cayman Islands with registered number 112331)

Multicurrency programme for the issuance of up to
£3,000,000,000 Guaranteed Wrapped Bonds
unconditionally and irrevocably guaranteed as to scheduled payments of principal and interest pursuant to financial guarantees issued by

MBIA UK Insurance Limited

(incorporated on 22 March 2002 with limited liability in England and Wales pursuant to the Companies Act 1985 and with registered number 04401508)

and

£3,000,000,000 Guaranteed Unwrapped Bonds
financing
Southern Water Services Limited

(incorporated in England and Wales with limited liability with registered number 2366670)

On 23 July 2003, Southern Water Services (Finance) Limited (the "**Issuer**"), entered into a multicurrency programme for the issuance of up to £3,000,000,000 Guaranteed **Wrapped** Bonds and £3,000,000,000 Guaranteed Unwrapped Bonds (the "**Programme**"). The Programme was last updated on 24 May 2005. This Prospectus supersedes the offering circular relating to the Programme dated 24 May 2005. This Prospectus does not affect any bonds issued under the Programme before the date of this Prospectus. The payment of all amounts owing in respect of the bonds issued under the Programme (the "**Bonds**") will be unconditionally and irrevocably guaranteed by Southern Water Services Limited ("**SWS**"), SWS Holdings Limited ("**SWSH**") and SWS Group Holdings Limited ("**SWSGH**") as described herein. SWS, the Issuer, SWSH and SWSGH are together referred to herein as the "Obligors". Neither SWSH nor SWSGH has any significant assets other than the shares in its respective subsidiary.

Application has been made to the Financial Services Authority in its capacity as competent authority under the Financial Services and Markets Act 2000 as amended ("**FSMA**") (the "**UK Listing Authority**" or "**UKLA**") for Bonds issued under the Programme during the period of twelve months after the date hereof, to be admitted to the official list of the UK Listing Authority (the "**Official List**") and to the London Stock Exchange plc (the "**London Stock Exchange**") for such Bonds to be admitted to trading on either the London Stock Exchange's Gilt-Edged and Fixed Interest Market (the "**Market**") or on the London Stock Exchange's Professional Securities Market ("**PSM**"). References in this Prospectus to Bonds being "**listed**" (and all related references) shall mean that such Bonds have been admitted to trading on the Market or the PSM and have been admitted to the Official List. The Market is a regulated market for the purposes of the Investment Services Directive 93/22/EC. The PSM is not a regulated market for the purposes of the Investment Services Directive 93/22/EC.

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

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

Please see Chapter 5 "Risk Factors" to read about certain factors you should consider before buying any Bonds.

Co-Arrangers

The Royal Bank of Scotland | **Citigroup**

Dealers

The Royal Bank of Scotland | **Citigroup**
Credit Suisse | **Morgan Stanley**

Prospectus dated 13 October 2006

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Under the Programme the Issuer may, subject to all applicable legal and regulatory requirements, from time to time issue Bonds in bearer and/or registered form (respectively "**Bearer Bonds**" and "**Registered Bonds**"). Copies of the Final Terms (as defined below) will be available (in the case of all Bonds) from the specified office set out below of Deutsche Trustee Company Limited as bond trustee (the "**Bond Trustee**"), (in the case of Bearer Bonds) from the specified office set out below of each of the Paying Agents (as defined below) and (in the case of Registered Bonds) from the specified office set out below of each of the Registrar and the Transfer Agent (each as defined below), provided that, in the case of Bonds which are not listed on any stock exchange, copies of the relevant Final Terms will only be available for inspection by the relevant Bondholders.

The maximum aggregate nominal amount of all Bonds from time to time outstanding under the Programme will not exceed £6,000,000,000 (or its equivalent in other currencies calculated as described herein), subject to increase as described herein.

Details of the aggregate principal amount, interest (if any) payable, the issue price and any other conditions not contained herein, which are applicable to each Tranche of each Sub-Class of each Class of each Series (all as defined below) will be set forth in a set of final terms (the "**Final Terms**") which, in the case of Bonds to be admitted to the Official List and to trading on the Market or the PSM, will be delivered to the UK Listing Authority and the London Stock Exchange on or before the relevant date of issue of the Bonds of such Tranche. The Issuer may also issue unlisted Bonds.

Bonds issued under the Programme will be issued in series (each a "**Series**") and in one or more of four classes (each a "**Class**"). The guaranteed wrapped Bonds will be designated as either "**Class A Wrapped Bonds**" or as "**Class B Wrapped Bonds**". The guaranteed unwrapped Bonds- will be designated as either "**Class A Unwrapped Bonds**" or "**Class B Unwrapped Bonds**". Each Class may comprise one or more sub-classes (each a "**Sub-Class**") with each Sub-Class pertaining to, among other things, the currency, interest rate and maturity date of the relevant Sub-Class. Each Sub-Class may be zero-coupon, fixed rate, floating rate or index-linked Bonds and may be denominated in sterling, euro or U.S. dollars (or in other currencies subject to compliance with applicable laws).

Each Class of Bonds is expected on issue to have the following credit ratings:

Class	**Standard & Poor's**	**Moody's**	**Fitch**
Class A Wrapped Bonds	AAA	Aaa	AAA
Class A Unwrapped Bonds	A-	A3	A-
Class B Wrapped Bonds	AAA	Aaa	AAA
Class B Unwrapped Bonds	BBB	Baa3	BBB

Class A Wrapped Bonds and Class B Wrapped Bonds will be unconditionally and irrevocably guaranteed as to scheduled payments of interest and principal (as adjusted for indexation, as applicable, but excluding any additional amounts relating to premium, prepayment or acceleration, accelerated amounts and Subordinated Coupon Amounts, as defined below (the "**FG Excepted Amounts**")) pursuant to Financial Guarantees (and the endorsements thereto) to be issued by MBIA UK Insurance Limited ("**MBIA**") as set out in Chapter 10 "*MBIA and its Financial Guarantees*" or, subject to the approval of the Dealers (and confirmation of no downgrade of the Wrapped Bonds (as defined below) then in issue from at least two of the Rating Agencies), pursuant to Financial Guarantees issued by other financial institutions (MBIA and each other such financial institution, a "**Financial Guarantor**"). The credit rating of such Class A Wrapped Bonds and such Class B Wrapped Bonds will be based upon the

financial strength of the relevant Financial Guarantor. None of the Class A Unwrapped Bonds or Class B Unwrapped Bonds will benefit from a Financial Guarantee or the guarantee of any other financial institution.

Each Sub-Class of Bearer Bonds may be represented initially by a Temporary Global Bond (as defined below), without interest coupons, which will be deposited with a common depositary for Euroclear and Clearstream, Luxembourg (as defined below) on or about the Issue Date (as defined below) of such Sub-Class. Each such Temporary Global Bond will be exchangeable for definitive securities in bearer form following the expiration of 40 days after the later of the commencement of the offering and the relevant Issue Date, upon certification as to non-U.S. beneficial ownership or to the effect that the holder is a U.S. person who purchased in a transaction that did not require registration under the Securities Act (as defined below) and as may be required by U.S. tax laws and regulations, as described in Chapter 8 "*The Bonds*" under "*Forms of the Bonds*". Ratings ascribed to all of the Bonds reflect only the views of Standard & Poor's, a division of The McGraw Hill companies ("**Standard & Poor's**"), Moody's Investors Service Limited ("**Moody's**") and Fitch Ratings Ltd. ("**Fitch**" and, together with Moody's and Standard & Poor's, the "**Rating Agencies**").

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

If any withholding or deduction for or on account of tax is applicable to the Bonds, payments of interest on, principal of and premium (if any) on, the Bonds will be made subject to such withholding or deduction, without the Issuer being obliged to pay any additional amounts as a consequence.

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

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

IMPORTANT NOTICE

This prospectus (the "**Prospectus**") comprises (i) a base prospectus for the purposes of Article 5.4 of Directive 2003/71/EC (the "**Prospectus Directive**") and for the purpose of giving information with regard to the Issuer and the other Obligors which, according to the particular nature of the Issuer and the Bonds, is necessary to enable investors to make an informed assessment of the assets and liabilities, financial position, profit and losses and prospects of the Issuer and (ii) listing particulars for the purposes of LR2.2.11 of the Listing Rules of the Financial Services Authority.

Each of the Issuer and the other Obligors accepts responsibility for the information contained in this Prospectus. To the best of the knowledge and belief of the Issuer and each of the other Obligors (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.

The information relating to The Royal Bank of Scotland plc and The Royal Bank of Scotland Group plc contained in Chapter 11 "Description Of Hedge Counterparties" has been accurately reproduced and as far as the Issuer is aware and is able to ascertain from such information, no facts have been omitted which would render the reproduced information inaccurate or misleading. The information relating to Citibank, N.A., Citigroup Inc. and their affiliates contained in Chapter 11 "Description Of Hedge Counterparties" has been accurately reproduced and as far as the Issuer is aware and is able to ascertain from such information, no facts have been omitted which would render the reproduced information inaccurate or misleading.

MBIA accepts responsibility for the information contained in Chapter 10 "MBIA and its Financial Guarantees" on pages 241 to 270 and in the paragraphs relating to MBIA under the headings "Significant or Material Change", "Litigation" and "Availability of Financial Statements" and "Auditors" in Chapter 14 "General Information" on pages 285 to 286 and in the financial statements of MBIA (together, the "**MBIA Information**"). To the best of the knowledge and belief of MBIA (which has taken all reasonable care to ensure that such is the case), the MBIA Information is in accordance with the facts and does not omit anything likely to affect the import of such information. MBIA accepts no responsibility for any other information contained in this Prospectus. Save for the MBIA Information, MBIA has not separately verified the information contained herein. No representation, warranty or undertaking, express or implied, is made and no responsibility or liability is accepted by MBIA as to the accuracy or completeness of any information contained in this Prospectus (other than the MBIA Information) or any other information supplied in connection with the Programme or distribution of any Bonds issued under the Programme.

This Prospectus is being distributed only to, and is directed only at, persons who (i) are outside the United Kingdom or (ii) are persons who have professional experience in matters relating to investments falling within Article 19(1) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (the "**Order**") or (iii) are high net worth entities, and other persons to whom it may lawfully be communicated, falling within Article 49(1) of the Order (all such persons together being referred to as "**relevant persons**") and in each case who do not constitute the public in the Cayman Islands. This Prospectus, or any of its contents, must not be acted on or relied on by persons who are not relevant persons. Any investment or investment activity to which this Prospectus relates is available only to, and any invitation, offer or agreement to subscribe, purchase or otherwise acquire such investments will be engaged in only with, relevant persons.

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

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

The Series of Wrapped Bonds issued on 23 July 2003 and 27 May 2005 have the benefit of Financial Guarantees issued by MBIA Assurance S.A. For any further Series of Wrapped Bonds issued under the Programme, a new Financial Guarantee dated as of the Issue Date of such Series of Wrapped Bonds will be entered into by MBIA or another Financial Guarantor in respect of such Bonds.

In the case of each Tranche of Wrapped Bonds, admission to the Official List and trading on the Market or the PSM is subject to the issue by MBIA or another Financial Guarantor of a Financial Guarantee in respect of such Tranche.

No person has been authorised to give any information or to make representations other than the information or the representations contained in this Prospectus in connection with the Issuer, any member of the SWS Financing Group (as defined below) or of the Group (as defined below), MBIA, or the offering or sale of the Bonds and, if given or made, such information or representations must not be relied upon as having been authorised by the Issuer, any member of the SWS Financing Group or of the Group, MBIA, the Dealers, the Bond Trustee or the Security Trustee. Neither the delivery of this Prospectus nor any offering or sale of Bonds made in connection herewith shall, under any circumstances, constitute a representation or create any implication that there has been no change in the affairs of the Issuer, any member of the SWS Financing Group or MBIA since the date hereof. Unless otherwise indicated herein, all information in this Prospectus is given as of the date of this Prospectus. This document does not constitute an offer of, or an invitation by, or on behalf of, the Issuer or any Dealer to subscribe for, or purchase, any of the Bonds.

None of the Dealers, the Financial Guarantors, the Bond Trustee or the Security Trustee nor any of the Hedge Counterparties, the Liquidity Facility Providers, the Authorised Credit Providers, the Agents, the Account Bank, the Standstill Cash Manager, the Mezzanine Facility Providers or the members of the Group (other than the Obligors) (each as defined below and, together, the "**Other Parties**") has separately verified the information contained herein (other than, in respect of MBIA, the MBIA Information). Accordingly, no representation, warranty or undertaking, express or implied, is made and no responsibility or liability is accepted by any Dealer, Financial Guarantor, the Bond Trustee or the Security Trustee or Other Party as to the accuracy or completeness of the information contained in this Prospectus or any other information supplied in connection with the Bonds or their distribution (other than, in respect of MBIA, the MBIA Information). The statements made in this paragraph are without prejudice to the respective responsibilities of the Issuer, the other Obligors and MBIA. Each person receiving this Prospectus acknowledges that such person has not relied on any Dealer, Financial Guarantor, the Bond Trustee or the Security Trustee or Other Party nor on any person affiliated with any of them in connection with its investigation of the accuracy of such information or its investment decision (other than, in respect of MBIA, the MBIA Information).

Neither the delivery of this Prospectus nor the offering, sale or delivery of any Bonds shall in any circumstances imply that the information contained herein concerning the Obligors or MBIA is correct at any time subsequent to the date hereof or that any other information supplied in connection with the Programme is correct or that there has been no adverse change in the financial position of the Issuer or

the other Obligors as of any time subsequent to the date indicated in the document containing the same. None of the Dealers, the Financial Guarantors, the Bond Trustee, the Security Trustee or the Other Parties expressly undertakes to review the financial condition or affairs of any of the Obligors during the life of the Programme or to advise any investor in the Bonds of any information coming to their attention. Investors should review, among other things, the most recently published documents incorporated by reference into this Prospectus when deciding whether or not to purchase any Bonds.

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, any Financial Guarantor, any member of the SWS Financing Group, any member of the Group, any Dealer, the Bond Trustee, the Security Trustee or any of the Other Parties that any recipient of this Prospectus should purchase any of the Bonds.

Each person contemplating making an investment in the Bonds must make its own investigation and analysis of the creditworthiness of the Issuer, the other Obligors and MBIA and its own determination of the suitability of any such investment, with particular reference to its own investment objectives and experience and any other factors which may be relevant to it in connection with such investment. A prospective investor who is in any doubt whatsoever as to the risks involved in investing in the Bonds should consult independent professional advisers.

The Bonds and any guarantees in respect thereof have not been and will not be registered, under the United States Securities Act of 1933, as amended (the "**Securities Act**") or with any securities regulatory authority of any state or other jurisdiction of the United States and may include Bonds in bearer form that are subject to U.S. tax law requirements. Subject to certain exemptions, the Bonds may not be offered or sold or, in the case of Bearer Bonds, delivered within the United States or to, or for the account or benefit of, U.S. persons (as defined in the Securities Act). The Bonds are being offered outside the United States in reliance on Regulation S under the Securities Act. See Chapter 13 "*Subscription and Sale*" below.

The distribution of this Prospectus and the offering, sale or delivery of the Bonds in certain jurisdictions may be restricted by law. Persons into whose possession this Prospectus comes are required by the Issuer, MBIA and the Dealers to inform themselves about and to observe any such restrictions. For a description of certain restrictions on offers and sales of the Bonds and on distribution of this Prospectus, see Chapter 13 "*Subscription and Sale*" below. This Prospectus does not constitute, and may not be used for the purposes of, an offer to or solicitation by any person to subscribe or purchase any Bonds in any jurisdiction or in any circumstances in which such an offer or solicitation is not authorised or is unlawful.

No invitation may be made to the public in the Cayman Islands to subscribe for any of the Bonds.

All references herein to "**pounds**", "**sterling**" or "**£**" are to the lawful currency of the United Kingdom, all references to "**$**", "**U.S.$**", "**U.S. dollars**" and "**dollars**" are to the lawful currency of the United States of America, and references to "**€**" or "**euro**" are to the single currency introduced at the start of the third stage of European Economic and Monetary Union pursuant to the Treaty establishing the European Community, as amended, from time to time.

In connection with the issue and distribution of any Tranche of Bonds, the Dealer (if any) disclosed as the stabilising manager in the applicable Final Terms or any person acting for him may over-allot (provided that, in the case of any Tranche of Bonds to be admitted to trading on the Market, the aggregate principal amount of Bonds allotted does not exceed 105 per cent. of the aggregate principal amount of the relevant Tranche) or effect transactions with a view to

supporting the market price of the Bonds of the Series of which such Tranche forms part, at a level higher than that which might otherwise prevail. However, there is no assurance that the stabilising manager or any agent of his will undertake stabilisation action. Any stabilisation action may begin on or after the date on which adequate public disclosure of the terms of the offer of the relevant Tranche of Bonds is made and, if begun, may be ended at any time, but it must end no later than the earlier of 30 days after the Issue Date of the relevant Tranche of Bonds and 60 days after the date of the allotment of the relevant Tranche of Bonds.

DOCUMENTS INCORPORATED BY REFERENCE

This Prospectus should be read and construed in conjunction with the audited non-consolidated financial statements of each of the Obligors for the financial years ended 31 March 2005 and 2006 and the audited consolidated annual financial statements and audited non-consolidated financial statements of MBIA for the financial years ended 31 December 2004 and 2005 together in each case with the audit report thereon, which have been previously published or are published simultaneously with this Prospectus and which have been approved by the Financial Services Authority or filed with it (see Chapter 14 "*General Information — Documents Available*" for a description of the financial statements currently available for each of the Obligors) save that any statement contained herein or in a document which is deemed to be incorporated by reference herein shall be deemed to be modified or superseded for the purpose of this Prospectus to the extent that a statement contained in any such subsequent document which is deemed to be incorporated by reference herein modifies or supersedes such earlier statement (whether expressly, by implication or otherwise). Any statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this Prospectus.

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

Each of the Obligors has undertaken to the Dealers in the Dealership Agreement (as defined in Chapter 13 "*Subscription and Sale*") to comply with Section 81 of the FSMA.

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

Copies of documents deemed to be incorporated by reference in this Prospectus may be viewed on the website of the Regulatory News Service operated by the London Stock Exchange at http://www.londonstockexchange.com/en-gb/pricesnews/marketnews/.

SUPPLEMENTARY PROSPECTUS

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

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

SUPPLEMENTARY LISTING PARTICULARS

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

If at any time any Issuer shall be required to prepare supplementary listing particulars pursuant to Section 81 of the FSMA, the Issuer shall prepare and make available an appropriate supplement to this Prospectus or a further prospectus which, in respect of any subsequent issue of Bonds to be listed on the Official List and admitted to trading on the PSM, shall constitute supplementary listing particulars as required by the UK Listing Authority and Section 81of the FSMA.

CHAPTER 1
THE PARTIES

The Issuer	Southern Water Services (Finance) Limited, a company incorporated in the Cayman Islands on 17 August 2001 with limited liability with registered number 112331, is the funding vehicle for raising funds to support the long term debt financing requirements of SWS. The Issuer is a 100% subsidiary of SWS.
SWS	Southern Water Services Limited, a company incorporated in England and Wales with limited liability (registered number 2366670) on 1 April 1989, which holds an Instrument of Appointment dated August 1989 under sections 11 and 14 of the Water Act 1989 (as in effect on 1 September 1989) under which the Secretary of State for the Environment appointed SWS as a water and sewerage undertaker under the WIA for the areas described in the Instrument of Appointment. SWSH owns 100% of the issued ordinary share capital in SWS.
SWSH	SWS Holdings Limited, a company incorporated in England and Wales with limited liability (registered number 04324499). SWSH is a 100% subsidiary of SWSGH.
SWSGH	SWS Group Holdings Limited, a company incorporated in England and Wales with limited liability (registered number 04324498). SWSGH is a 100% subsidiary of Southern Water Services Group Limited.
Guarantors	Pursuant to the terms of the Security Agreement, SWSH and SWSGH each guarantee the obligations of each other and of SWS and the Issuer under each Finance Document in favour of the Security Trustee. In addition, SWS and the Issuer each guarantee the obligations of each other (but not those of SWSH and SWSGH) under each Finance Document in favour of the Security Trustee. SWSH, SWSGH, SWS and the Issuer are collectively referred to herein as the "**Guarantors**" and each a "**Guarantor**".
SWS Financing Group	The SWS Financing Group comprises SWSGH, SWSH, SWS, the Issuer and the Pension Companies (as defined below).
SWSG	Southern Water Services Group Limited, a company incorporated in England and Wales with limited liability (registered number 04374956), whose registered office is at Southern House, Yeoman Road, Worthing, West Sussex BN13 3NX. Southern Water Services Group Limited is a 100% subsidiary of SWI.
SWI	Southern Water Investments Limited, a company incorporated in England and Wales (registered number 04650294), whose registered office is at Southern House, Yeoman Road,

	Worthing, West Sussex BN13 3NX and which is the ultimate holding company of the SWS Financing Group. SWI owns 150,000 participating cumulative redeemable preference shares 2038 of 1p each (the "**Class A2 Preference Shares**") in the capital of SWS. SWI is a 100 per cent. subsidiary of SWC.
SWC	Southern Water Capital Limited, a company incorporated in England and Wales (registered number 04608528) whose registered office is c/o Hackwood Secretaries Limited, One Silk Street, London EC2Y 8HQ. SWC owns the Class A1 Preference Shares and the Class B Preference Shares.
Group	SWI and its Subsidiaries from time to time.
Co-Arrangers	The Royal Bank of Scotland plc and Citigroup Global Markets Limited are the Co-Arrangers of the Programme.
Dealers	The Royal Bank of Scotland plc, Citigroup Global Markets Limited, Credit Suisse First Boston (Europe) Limited and Morgan Stanley & Co. International Limited will act as dealers (together with any other dealer appointed from time to time by the Issuer and the other Guarantors, "**Dealers**") either generally with respect to the Programme or in relation to a particular Tranche, Sub-Class, Class or Series of Bonds.
Financial Guarantors	MBIA Assurance S.A., as initial financial guarantor (in such capacity, the "**Initial Financial Guarantor**") under the terms of various financial guarantees (the "**Initial Financial Guarantees**") which it has issued in respect of Class A Wrapped Bonds issued on 23 July 2003 (the "**Initial Issue Date**") and on 27 May 2005. It is expected that if there is a tap issue of the Bonds issued on the Initial Issue Date or on 27 May 2005 and which have the benefit of an Initial Financial Guarantee, the relevant Initial Financial Guarantees will be novated by MBIA Assurance S.A. to MBIA UK Insurance Limited ("**MBIA**"). MBIA may agree to issue a financial guarantee in respect of further Class A Wrapped Bonds (subject to the satisfaction of certain conditions precedent contained in the CP Agreement prior to the issue of such further Class A Wrapped Bonds) in favour of the Bond Trustee, unconditionally and irrevocably guaranteeing the scheduled payment of interest and principal (as adjusted for indexation, as applicable, but excluding the FG Excepted Amounts) in respect of such Class A Wrapped Bonds. (See Chapter 10 "*MBIA and its Financial Guarantees*" under "*MBIA UK Insurance Limited – MBIA Financial Guarantee*").
	MBIA is under no obligation to issue further Financial Guarantees. The Issuer may arrange for such other financial guarantee companies (each, together with the Initial Financial Guarantor and MBIA, a "**Financial Guarantor**"), in addition to the Initial Financial Guarantor and MBIA, to issue Financial Guarantees in respect of further Tranches or Sub-Classes of

Class A Wrapped Bonds and/or Class B Wrapped Bonds or in respect of other Wrapped Debt issued or raised under an Authorised Credit Facility.

Hedge Counterparties

The Royal Bank of Scotland plc acting through its office at 135 Bishopsgate London EC2M 3UR and Citibank, N.A., London branch acting through its office at Citigroup Centre, Canada Square, Canary Wharf, London E14 5LB (together the "**Existing Hedge Counterparties**" and, together with any counterparties to future Hedging Agreements, the "**Hedge Counterparties**"). The Existing Hedge Counterparties are under no obligation to enter into any further Treasury Transactions.

Bond Trustee

Deutsche Trustee Company Limited (or any successor trustee appointed pursuant to the Bond Trust Deed) acts as trustee (the "**Bond Trustee**") for and on behalf of the holders of each Class of Bonds of each Series (each a "**Bondholder**").

Mezzanine Facility Provider

SWC (as the current "**Mezzanine Facility Provider**") has provided the Issuer with a £127,200,000 senior mezzanine credit facility and a £106,000,000 junior mezzanine credit facility (respectively the "**Senior Mezzanine Facility**" and the "**Junior Mezzanine Facility**" and together the "**Mezzanine Facilities**"), which it acquired from Royal Bank Investments Limited acting through its office at 280 Bishopsgate, London EC2M 4RB and a syndicate of lenders (the "**Initial Mezzanine Facility Providers**").

Security Trustee

Deutsche Trustee Company Limited (or any successor trustee appointed pursuant to the STID) acts as security trustee for itself and on behalf of the Secured Creditors (as defined below) (the "**Security Trustee**") and holds, and will be entitled to enforce, the Security (as defined below) subject to the terms of the STID (as defined below).

Secured Creditors

The Secured Creditors comprise any person who is a party to, or has acceded to, the STID as a Secured Creditor.

DSR Liquidity Facility Providers

The Royal Bank of Scotland plc acting through its office at 135 Bishopsgate, London EC2M 3UR and Barclays Bank plc (the "**Existing DSR Liquidity Facility Providers**") provide the Issuer with a 364-day revolving credit facility for interest requirements on the Class A Debt and, within certain limits, for interest requirements on the Class B Debt.

O&M Reserve Facility Provider

A provider of a liquidity facility pursuant to an O&M Reserve Facility Agreement to fund SWS's operating and maintenance expenditure, which, among others, the Issuer and such O&M Reserve Facility Provider may enter into from time to time.

Authorised Credit Providers

RBS and a syndicate of banks (the "**Initial RCF Providers**") provide SWS with revolving credit facilities to fund the working capital and capital expenditure requirements of SWS

	until 23 July 2008. Artesian Finance II plc and Artesian Finance plc have made index-linked advances to the Issuer. RBS and Bayerische Landesbank, London Branch (the "**Second RCF Providers**") provide SWS with a revolving credit facility to fund the prepayment of advances under the Third Issuer/SWS Loan Agreement or to fund the working capital expenses of SWS.
Paying Agents	Deutsche Bank AG, London Branch acts and will act as principal paying agent (the "**Principal Paying Agent**") and, together with any other paying agents appointed by the Issuer, the "**Paying Agents**") to provide certain issue and paying agency services to the Issuer in respect of the Bearer Bonds.
Agent Bank	Deutsche Bank AG, London Branch acts as agent bank (the "**Agent Bank**") under the Agency Agreement.
Account Bank	National Westminster Bank Plc, acting through its office at 27 South Street, Worthing, West Sussex BN11 3AR or any person for the time being acting as Account Bank (pursuant to the Account Bank Agreement). National Westminster Bank Plc is a company incorporated in England and Wales with registered number 929027 and has its registered office at 135 Bishopsgate, London EC2M 3UR. National Westminster Bank Plc is part of the RBS Group.
Cash Manager	SWS acts, or during a Standstill Period The Royal Bank of Scotland plc (the "**Standstill Cash Manager**") will act, pursuant to the terms of the cash management provisions of the CTA as cash manager in respect of moneys credited from time to time to the Accounts (as defined below).
Registrar and Transfer Agent	Deutsche Bank AG, London Branch will act as transfer agent (the "**Transfer Agent**") and will provide certain transfer agency services to the Issuer in respect of the Registered Bonds. Deutsche Bank Luxembourg S.A. will act as registrar (the "**Registrar**") and will provide certain registrar services to the Issuer in respect of the Registered Bonds.

CHAPTER 2
OVERVIEW OF THE PROGRAMME

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

Description	Guaranteed Bond Programme.
Programme Size	Up to £6,000,000,000 (or its equivalent in other currencies) aggregate nominal amount of Bonds outstanding at any time.
Issuance in Classes	Bonds issued under the Programme have been and will be issued in Series, with each Series belonging to one of four Classes. The Wrapped Bonds are and will be designated as either Class A Wrapped Bonds or Class B Wrapped Bonds. The Unwrapped Bonds are and will be designated as one of Class A Unwrapped Bonds or Class B Unwrapped Bonds. Each Class comprises or will comprise one or more Sub-Classes of Bonds and each Sub-Class can be issued in one or more Tranches, the specific terms of each Tranche of a Sub-Class being identical in all respects, save for the issue dates, interest commencement dates and/or issue prices, to the terms of the other Tranches of such Sub-Class. The specific terms of each Tranche of Bonds are and will be set out in the applicable Final Terms.
Issue Dates	23 July 2003 (the "**Initial Issue Date**"), 27 May 2005 and thereafter the date of issue of a Tranche of Bonds as specified in the relevant Final Terms (each an "**Issue Date**").
Certain Restrictions	Each issue of Bonds denominated in a currency in respect of which particular laws, guidelines, regulations, restrictions or reporting requirements apply will only be issued in circumstances which comply with such laws, guidelines, regulations, restrictions or reporting requirements from time to time including the restrictions applicable at the date of this Prospectus. See Chapter 13 "*Subscription and Sale*". **Bonds with a maturity of less than one year** Bonds having a maturity of less than one year from the date of issue will constitute deposits for the purposes of the prohibition on accepting deposits contained in section 19 of the FSMA unless they are issued to a limited class of professional investors and have a denomination of at least £100,000 or its equivalent. See Chapter 13 "*Subscription and Sale*".
Distribution	Bonds have been and may be distributed by way of private or public placement and in each case on a syndicated or non-syndicated basis.

Currencies	Euro, Sterling, U.S. dollars and, subject to any applicable legal or regulatory restrictions, any other currency agreed between the Issuer and the relevant Dealer.
Redenomination	The applicable Final Terms may provide that certain Bonds may be redenominated in euro. The relevant provisions applicable to any such redenomination will be contained in Condition 19 (*European Economic and Monetary Union*), as amended by the applicable Final Terms.
Maturities	Such maturities as may be agreed between the Issuer and the relevant Dealer, subject to such minimum or maximum maturities as may be allowed or required from time to time by the relevant central bank (or equivalent body) or any laws or regulations applicable to the Issuer or the relevant Specified Currency (as defined in the Conditions).
Issue Price	Bonds have been and may be issued on a fully-paid or a partly-paid basis and at an issue price which is at par or at a discount to, or premium over, par.
Interest	Bonds are and will, unless otherwise specified in the relevant Final Terms, be interest-bearing and interest is or will be calculated (unless otherwise specified in the relevant Final Terms) on the Principal Amount Outstanding (as defined in the Conditions) of such Bond. Interest accrues or will accrue at a fixed or floating rate (plus, in the case of Indexed Bonds, amounts in respect of indexation) and is or will be payable in arrear, as specified in the relevant Final Terms, or on such other basis and at such rate as may be so specified. Interest is or will be calculated on the basis of such Day Count Fraction (as defined in the Conditions) as may be agreed between the Issuer and the relevant Dealer as specified in the relevant Final Terms.
Form of Bonds	The Series 1 Bonds and Series 2 Bonds have been issued under the Programme in bearer form. Each further Sub-Class of Bonds will be issued in bearer or registered form as described in Chapter 8 "*The Bonds*". Registered Bonds will not be exchangeable for Bearer Bonds.
Fixed Rate Bonds	Fixed Rate Bonds bear interest at a fixed rate of interest payable on such date or dates as may be agreed between the Issuer and the relevant Dealer and on redemption, as specified in the relevant Final Terms.
Floating Rate Bonds	Floating Rate Bonds bear interest at a rate determined: (i) on the same basis as the floating rate under a notional interest rate swap transaction in the relevant Specified Currency governed by an agreement incorporating the 2000 ISDA Definitions (as published by the International Swaps and Derivatives Association, Inc., and as amended and updated as at the Issue Date of the first Tranche of the Bonds of the relevant Sub-Class); or

	(ii) on the basis of a reference rate appearing on the agreed screen page of a commercial quotation service; or (iii) on such other basis as may be agreed between the Issuer and the relevant Dealer. The margin (if any) relating to such floating rate has been or will be agreed between the Issuer and the relevant Dealer for each Sub-Class of Floating Rate Bonds.
Indexed Bonds	Payments (whether in respect of principal or interest and whether at maturity or otherwise) in respect of Indexed Bonds (including Limited Indexed Bonds as defined in Condition 7(a) (*Indexation – Definitions*)) are and may be calculated in accordance with Condition 7 by reference to the UK Retail Price Index or such other index and/or formula as the Issuer and the Relevant Dealer may agree (as specified in the relevant Final Terms).
Interest Payment Dates	Interest in respect of Fixed Rate Bonds is or will be payable annually in arrear, in respect of Floating Rate Bonds is or will be payable quarterly in arrear and in respect of Indexed Bonds is or will be payable semi-annually in arrear (or, in each case, as otherwise specified in the relevant Final Terms).
Dual Currency Bonds	Payments (whether in respect of principal or interest and whether at maturity or otherwise) in respect of Dual Currency Bonds will be made in such currencies, and based on such rates of exchange, as the Issuer and the relevant Dealer may agree.
Zero Coupon Bonds	Zero Coupon Bonds will be offered and sold at a discount to their nominal amount and will not bear interest.
Partly Paid Bonds	Partly Paid Bonds will be issued in the amount as specified in the relevant Final Terms and further instalments will be payable in the amounts and on the dates as specified in the relevant Final Terms.
Instalment Bonds	The applicable Final Terms may provide that Bonds may be redeemable in two or more instalments of such amounts and on such dates as are indicated in the applicable Final Terms.
Redemption	The applicable Final Terms indicate or will indicate either that the relevant Bonds cannot be redeemed prior to their stated maturity (other than in specified instalments, or for taxation reasons if applicable, or following an Index Event or an Event of Default) or that such Bonds will be redeemable at the option of the Issuer and/or the Bondholders upon giving notice to the Bondholders or the Issuer, as the case may be, on a date or dates specified prior to such stated maturity and at a price or prices and on such other terms as may be agreed between the Issuer and the relevant Dealer, in each case as set out in the applicable Final Terms.

Redemption for Index Event, Taxation or Other Reasons	Upon the occurrence of certain index events (as set out in Condition 8(c) (*Redemption for Index Event, Taxation or Other Reasons*)), the Issuer may redeem the Indexed Bonds at their Principal Amount Outstanding together with accrued but unpaid interest and amounts in respect of indexation. No single Sub-Class of Indexed Bonds may be redeemed in these circumstances unless all the other Sub-Classes of Indexed Bonds are also redeemed. In addition, in the event of the Issuer becoming obliged to make any deduction or withholding from payments in respect of the Bonds (although the Issuer will not be obliged to pay any additional amounts in respect of such deduction or withholding) the Issuer may (a) use its reasonable endeavours to arrange for the substitution of another company incorporated in an alternative jurisdiction (subject to certain conditions as set out in Condition 8(c) (*Redemption for Index Event, Taxation or Other Reasons*) of the Bonds) and, failing this, (b) redeem (subject to certain conditions as set out in Condition 8(c) (*Redemption for Index Event, Taxation or Other Reasons*) of the Bonds) all (but not some only) of the Bonds at their Principal Amount Outstanding (plus, in the case of Indexed Bonds, amounts in respect of indexation) together with accrued but unpaid interest. No single Class or Sub-Class of Bonds may be redeemed in these circumstances unless all the other Classes and Sub-Classes of Bonds are also redeemed in full at the same time. In the event of SWS electing to prepay an advance (in whole or in part) under an Issuer/SWS Loan Agreement, the Issuer shall be obliged to redeem all or the relevant part of the corresponding Sub-Class of Bonds or the proportion of the relevant Sub-Class which the proposed prepayment amount bears to the amount of the relevant advance under the relevant Issuer/SWS Loan Agreement Bonds having a maturity of less than one year from the date of issue are subject to restrictions on their denomination and distribution. See "*Certain Restrictions – Bonds with a maturity of less than one year*" above. The Financial Guarantors have not and will not guarantee any of the amounts payable by the Issuer upon an early redemption, and their obligation is or will be to continue to make payments in respect of the Bonds pursuant to the relevant Financial Guarantee on the dates on which such payments would have been required to be made had such early redemption not occurred. The Issuer shall only be permitted to pay Early Redemption Amounts to the extent that in so doing it will not cause an Event of Default to occur or subsist.

Denomination of Bonds	Bonds have been and will be issued in such denominations as were or may be agreed between the Issuer and the relevant Dealer save that (i) in the case of any Bonds which are to be admitted to trading on a regulated market within the European Economic Area or offered to the public in a Member State of the European Economic Area in circumstances which require the publication of a prospectus under the Prospectus Directive, the minimum denomination shall be €50,000 (or its equivalent in any other currency as at the date of issue of the Bonds); and (ii) in any other case, the minimum denomination of each Bond will be such as may be allowed or required from time to time by the relevant central bank (or equivalent body) or any laws or regulations applicable to the relevant Specified Currency. See "*Certain Restrictions – Bonds with a maturity of less than one year*" above.
Taxation	Payments in respect of Bonds or under the relevant Financial Guarantee are and will be made without withholding or deduction for, or on account of, any present or future taxes, duties, assessments or governmental charges of whatever nature imposed or levied by or on behalf of any jurisdiction, unless and save to the extent that the withholding or deduction of such taxes, duties, assessments or governmental charges is required by law. In that event and to that extent, the Issuer and, to the extent there is a claim under the relevant Financial Guarantee, the relevant Financial Guarantor will make payments subject to the appropriate withholding or deduction. No additional amounts will be paid by the Issuer or the Guarantors or, to the extent there is a claim under the relevant Financial Guarantee, by the relevant Financial Guarantor in respect of any withholdings or deductions, unless otherwise specified in the applicable Final Terms.
Status of the Bonds	The Bonds in issue constitute and any future Bonds issued under the Programme will constitute secured obligations of the Issuer. Each Class of Bonds ranks *pari passu* without preference or priority in point of security amongst themselves. The Bonds represent the right of the holders of such Bonds to receive interest and principal payments from (a) the Issuer in accordance with the terms and conditions of the Bonds (the "**Conditions**") and the trust deed dated 23 July 2003 as amended from time to time (the "**Bond Trust Deed**") entered into by the Obligors, MBIA Assurance S.A. and the Bond Trustee in connection with the Programme and (b) in the case of the Wrapped Bonds only, the relevant Financial Guarantor in certain circumstances in accordance with the relevant Financial Guarantee. The Class A Wrapped Bonds and the Class A Unwrapped Bonds in issue rank, and any further Class A Wrapped Bonds and Class A Unwrapped Bonds issued under the Programme

will rank, *pari passu* with respect to payments of interest and principal. However, only the Class A Wrapped Bonds have and will have the benefit of the relevant Financial Guarantee. All claims in respect of the Class A Wrapped Bonds and the Class A Unwrapped Bonds will rank in priority to payments of interest and principal due on all Class B Wrapped Bonds and Class B Unwrapped Bonds.

The Class B Unwrapped Bonds in issue rank, and any Class B Wrapped Bonds and any further Class B Unwrapped Bonds issued under the Programme will rank, *pari passu* with respect to payments of interest and principal. However, only the Class B Wrapped Bonds will have the benefit of the relevant Financial Guarantee.

Covenants

The representations, warranties, covenants (positive, negative and financial) and events of default which apply and will apply to, among other things, the Bonds are set out in a common terms agreement dated 23 July 2003 (the "**CTA**", see Chapter 7 "*Summary of the Financing Agreements*" under "*Common Terms Agreement*").

Guarantee and Security

The Bonds in issue are, and further Bonds issued under the Programme will be, unconditionally and irrevocably guaranteed and secured by each of SWS, SWSGH and SWSH pursuant to a guarantee and security agreement (the "**Security Agreement**") entered into by each such Obligor in favour of the Security Trustee over the entire property, assets, rights and undertaking of each such Obligor (the "**Security**"), in the case of SWS to the extent permitted by the WIA and Licence. Each such guarantee constitutes a direct, unconditional and secured obligation of each such Obligor. The Security is held by the Security Trustee on trust for the Secured Creditors (as defined below) under the terms of the Security Agreement, subject to the terms of the STID (as defined below).

Inter-creditor Arrangements

The Secured Creditors and each Obligor are each party to a security trust and intercreditor deed (the "**STID**"), which regulates, among other things, (i) the claims of the Secured Creditors; (ii) the exercise and enforcement of rights by the Secured Creditors; (iii) the rights of the Secured Creditors to instruct the Security Trustee; (iv) the rights of the Secured Creditors during the occurrence of an Event of Default; (v) the Entrenched Rights and Reserved Matters of each Secured Creditor; and (vi) the giving of consents and waivers and the making of amendments by the Secured Creditors. See Chapter 7 "*Summary of the Financing Agreements*" under "*Security Trust and Intercreditor Deed*".

Status of Financial Guarantees in relation to Wrapped Bonds	Each Financial Guarantee issued in favour of the Bond Trustee in relation to each Sub-Class of Wrapped Bonds is or will be a direct, unsecured obligation of the relevant Financial Guarantor which ranks or will rank at least *pari passu* with all other unsecured obligations of such Financial Guarantor, save for such obligations as may be preferred by provisions of law that are both mandatory and of general application, pursuant to which the relevant Financial Guarantor guarantees or will guarantee the timely payment of interest and principal (other than the FG Excepted Amounts) on the relevant Sub-Class of Wrapped Bonds.
Reimbursement	The Issuer is or will be obliged, pursuant to the terms of a guarantee and reimbursement deed or an insurance and indemnity agreement with the relevant Financial Guarantor in respect of any Sub-Class or Sub-Classes of Wrapped Bonds or any other Wrapped Debt, among other things, to reimburse such Financial Guarantor in respect of payments made by it under the relevant Financial Guarantee or Financial Guarantees of such Sub-Class or Sub-Classes of Bonds. Each such Financial Guarantor will be subrogated to the rights of the relevant Class A Wrapped Bondholders or Class B Wrapped Bondholders or Authorised Credit Provider, as the case may be, against the Issuer in respect of any payments made under such Financial Guarantees. See Chapter 7 "*Summary of the Financing Agreements*" under "*Financial Guarantor Documents*". SWS guarantees such reimbursement obligations of the Issuer.
Authorised Credit Facilities	Subject to certain conditions being met, the Issuer and (for certain indebtedness) SWS are permitted to incur indebtedness under authorised credit facilities (each an "**Authorised Credit Facility**") with an Authorised Credit Provider, providing loan, hedging and other facilities (including Financial Guarantees) which may rank *pari passu* with the Class A Bonds, the Class B Bonds, the Senior Mezzanine Debt or the Junior Mezzanine Debt. Each Authorised Credit Provider is or will become party to the CTA and the STID and may have voting rights thereunder. See Chapter 7 "*Summary of the Financing Agreements*".
DSR Liquidity Facility	The DSR Liquidity Facility Providers make available to the Issuer a credit facility for the purpose of meeting certain shortfalls in revenues for the Issuer to meet, among other things, its obligations to pay interest on the Bonds. The Issuer is obliged, pursuant to the CTA, to maintain through a DSR Liquidity Facility (or DSR Liquidity Facilities) and/or amounts in the Debt Service Reserve Account an amount or amounts which is/are at least equal to the aggregate of projected interest payments on the Class A Debt and the Class B Debt for the succeeding 12 months.

O&M Reserve and O&M Reserve Facility	SWS has established a reserve in the amount of approximately 44.1 million (as at 31 March 2006) in the O&M Reserve Account of SWS. The principal amount credited to the O&M Reserve Account (the "**O&M Reserve**") may only be used by SWS for the purpose of meeting its operating and maintenance expenses. O&M Reserve Facility Providers may additionally make available to the Issuer a liquidity facility, the proceeds from which will be on-lent by the Issuer to SWS for the purpose of meeting SWS' operating and maintenance expenses.
Listing	The Bonds issued on the Initial Issue Date and all subsequent issues under the Programme have been admitted to the Official List and admitted to trading on the Market. Application has been made to admit further Bonds issued under the Programme to the Official List and to admit them to trading on the Market or the PSM. The Bonds may also be listed on such other or further stock exchange(s) as may be agreed between the Issuer and the relevant Dealer in relation to each Series. Unlisted Bonds may also be issued. The applicable Final Terms will state whether or not the relevant Bonds are to be listed and, if so, on which stock exchange(s).
Ratings	The ratings assigned to Class A Wrapped Bonds in issue are, and in respect of any further Class A Wrapped Bonds and Class B Wrapped Bonds to be issued under the Programme will be, based solely on the debt rating of the Initial Financial Guarantor, MBIA and/or any other Financial Guarantor appointed in relation to any further Wrapped Bonds issued under the Programme and reflect only the views of the Rating Agencies. The ratings assigned to the Class A Unwrapped Bonds and the Class B Unwrapped Bonds by the Rating Agencies reflect only the views of the Rating Agencies. The initial ratings of a Series of Bonds will be specified in the relevant Final Terms. A rating is not a recommendation to buy, sell or hold securities and will depend, among other things, on certain underlying characteristics of the business and financial condition of SWS or, in the case of the Class A Wrapped Bonds and/or Class B Wrapped Bonds, of the Initial Financial Guarantor, MBIA and/or any other applicable Financial Guarantor from time to time. A rating may be subject to suspension, change or withdrawal at any time by the assigning Rating Agency.
Governing Law	The Bonds in issue are and any further Bonds issued under the Programme will be governed by, and construed in accordance with, English law.

Selling Restrictions	There are restrictions on the offer, sale and transfer of the Bonds in the United States, the United Kingdom, the Cayman Islands and such other restrictions as may be required in connection with the offering and sale of a particular Sub-Class of Bonds. See Chapter 13 "*Subscription and Sale*".
Investor Information	SWS is required to produce an investors' report (the "**Investors' Report**") semi-annually to be delivered within 120 days from 31 March or 60 days from 30 September of each year. Such Investors' Report will include, among other things: (i) a general overview of the SWS business in respect of the six month period ending on the immediately preceding Calculation Date; (ii) the calculations of the Class A ICR, Class A Adjusted ICR and the Senior Adjusted ICR for each Test Period (historic and projected); (iii) the ratio of Net Cash Flow minus Capital Maintenance Expenditure to Class A Debt Interest for the twelve month period ending on such Calculation Date; (iv) the Class A RAR and Senior RAR (historic and projected); and (v) reasonable detail of the computations of these financial ratios. Each such Investors' Report will be made available by SWS and the Issuer to the Secured Creditors, including the Bondholders on SWS' website. SWS is also required to make available unaudited interim financial statements and audited financial statements, within 60 days of 30 September and 120 days of 31 March, respectively and, in any event within five Business Days of the date on which they are made available. SWS will also place certain additional information on its website, as and when available. This will include, among other things, the most recently published: (a) annual charges scheme for SWS, with details of tariffs; (b) a summary of SWS' strategic business plan at each Periodic Review; (c) SWS' current Procurement Plan (as defined below) (if any); (d) SWS' annual drinking water quality report; (e) SWS' annual environment report; (f) SWS' annual conservation and access report; and (g) such other periodic information compiled by SWS for Ofwat.

CHAPTER 3
SUMMARY FINANCING STRUCTURE

History and Background

On 7 May 2003, SWI completed its acquisition of the entire issued ordinary share capital of the Issuer from First Aqua Holdings Limited. The Issuer completed its acquisition of Southern Water (NR) Limited and its subsidiaries (including SWS) from Scottish Power UK plc in April 2002 (the "**First Aqua Acquisition**").

SWI is controlled by Southern Water Capital Limited ("**SWC**") (the largest shareholder in which is Royal Bank Investments Limited, a subsidiary of The Royal Bank of Scotland plc) which holds 100 per cent. of the issued ordinary share capital of SWI following the acquisition of 25 per cent. of the issued ordinary share capital of SWI in April 2006 which was held by Veolia Water UK PLC indirectly through Veolia Water Investment Limited. Concurrent with this acquisition of issued ordinary share capital, SWC also acquired (i) the Class A1 Preference Shares and Class B Preference Shares and (ii) the Senior Mezzanine Facilities and Junior Mezzanine Facilities (together the "**SWC Acquisition**"). SWC raised a £175,000,000 senior debt facility and a £127,200,000 Senior Mezzanine Facility and a £106,000,000 Junior Mezzanine Facility and issued subordinated loan notes to fund the SWC Acquisition.

Immediately before the first issue of Bonds on the Initial Issue Date, SWI implemented a corporate reorganisation to facilitate the creation of the SWS Financing Group within the Group. This involved the Issuer transferring its shares in its then immediate subsidiary, SWSG, to SWI; SWI transferring its shares in the Issuer to SWS; and SWS assuming certain existing intra-group indebtedness that SWSG incurred to the Issuer in connection with the First Aqua Acquisition.

The SWS Financing Group consists of SWSGH, SWSH, SWS, the Issuer and the Pension Companies (which act as trustees of two pension schemes in which SWS participates). The sole purpose for the creation of the SWS Financing Group was to facilitate the refinancing and future financing of the operating and capital requirements of SWS through the issuance of Bonds, other instruments of financial indebtedness and credit facilities, from time to time, incurred by the Issuer and SWS. The Issuer may on-lend the proceeds of Financial Indebtedness incurred by it to SWS pursuant to the Issuer/SWS Loan Agreements.

The Initial Issue Date

On the Initial Issue Date, the Issuer issued the following Sub-Classes of Bonds:

(i) £350,000,000 Series 1 Sub-Class A1 Wrapped 6.192 per cent. Bonds due March 2029;

(ii) £150,000,000 Series 1 Sub-Class A2a Wrapped Index-Linked Bonds due March 2034;

(iii) £35,000,000 Series 1 Sub-Class A2b Wrapped Limited Index Bonds due March 2034;

(iv) U.S.$483,000,000 Series 1 Sub-Class A3 Wrapped Floating Rate Bonds due March 2007;

(v) £350,000,000 Series 1 Sub-Class A4 Unwrapped 6.640 per cent. Bonds due March 2026;

(vi) £150,000,000 Series 1 Sub-Class A5 Unwrapped Index-Linked Bonds due March 2023;

(vii) £120,000,000 Series 1 Sub-Class A6 Unwrapped Step-Up Floating Rate Bonds due March 2013; and

(viii) £250,000,000 Series 1 Sub-Class B1 Unwrapped Step-Up Fixed/Floating Rate Bonds due March 2038

(together, the "**Series 1 Bonds**").

The Issuer applied the proceeds of the Series 1 Bonds, the Mezzanine Facilities and the Initial Term Facility to settle certain termination payments under existing hedging contracts terminated on or prior to the Initial Issue Date and to make advances to SWS under the Initial Issuer/SWS Loan Agreement to enable SWS to repay on the Initial Issue Date all existing intercompany indebtedness owed by it to the Issuer. The Issuer applied the repayment proceeds of the existing intercompany indebtedness owed to it by SWS among other things (i) to repay its then existing indebtedness to SWI, (ii) to pay all amounts outstanding under the term facility of the Bridge Facility Agreement and (iii) to meet certain transaction fees and expenses.

SWS applied the proceeds of its issue of SWS Preference Shares on the Initial Issue Date (together with any monies received under the Initial Issuer/SWS Loan Agreement and not required to be applied in repayment of existing indebtedness to the Issuer): (i) to discharge the obligations of SWS under the Bridge Facility Agreement, (ii) to fund the Capex Reserve Account and its O&M Reserve Account, (iii) to make an initial payment to the Debt Service Payment Account, (iv) to pay certain transaction fees and expenses, and (v) for general corporate purposes.

The advances made by the Issuer to SWS under the Initial Issuer/SWS Loan Agreement on the Initial Issue Date reflect the corresponding amount and terms of borrowing by the Issuer of each Sub-Class of Series 1 Bonds and each borrowing under the Mezzanine Facility Agreements and the Initial Term Facility on the Initial Issue Date and, to the extent that such borrowing was hedged under a Hedging Agreement, the terms of such Hedging Agreement.

The U.S.$483,000,000 Series 1 Sub-Class A3 Wrapped Floating Rate Bonds due March 2007 and the £120,000,000 Series 1 Sub-Class A6 Unwrapped Step-Up Floating Rate Bonds due March 2013 were redeemed on 30 June 2005 (the "**Series 1 Redeemed Bonds**").

The Second Issue Date

On 5 July 2004, Artesian advanced the Second Artesian Term Facility to the Issuer.

The advance made by the Issuer to SWS under the Second Issuer/SWS Loan Agreement reflects the corresponding amount and terms of borrowing by the Issuer under the Second Artesian Term Facility.

The Third Issue Date

On the Third Issue Date, the Issuer issued the following Sub-Classes of Bonds:

(i) £350,000,000 Series 2 Sub-Class A7 Wrapped 5.00 per cent. Bonds due March 2021; and

(ii) £150,000,000 Series 2 Sub-Class A8 Wrapped 5.00 per cent. Bonds due March 2041,

(together, the "**Series 2 Bonds**").

The advances made by the Issuer to SWS under the Third Issuer/SWS Loan Agreement reflect the corresponding amount and terms of borrowing by the Issuer of each Sub-Class of Series 2 Bonds. SWS applied the advances made by the Issuer under the Third Issuer/SWS Loan Agreement to, among other things, prepay the advances made by the Issuer to SWS under the Initial Issuer/SWS Loan Agreement corresponding to the Series 1 Redeemed Bonds.

FIGURE 1 – OWNERSHIP STRUCTURE

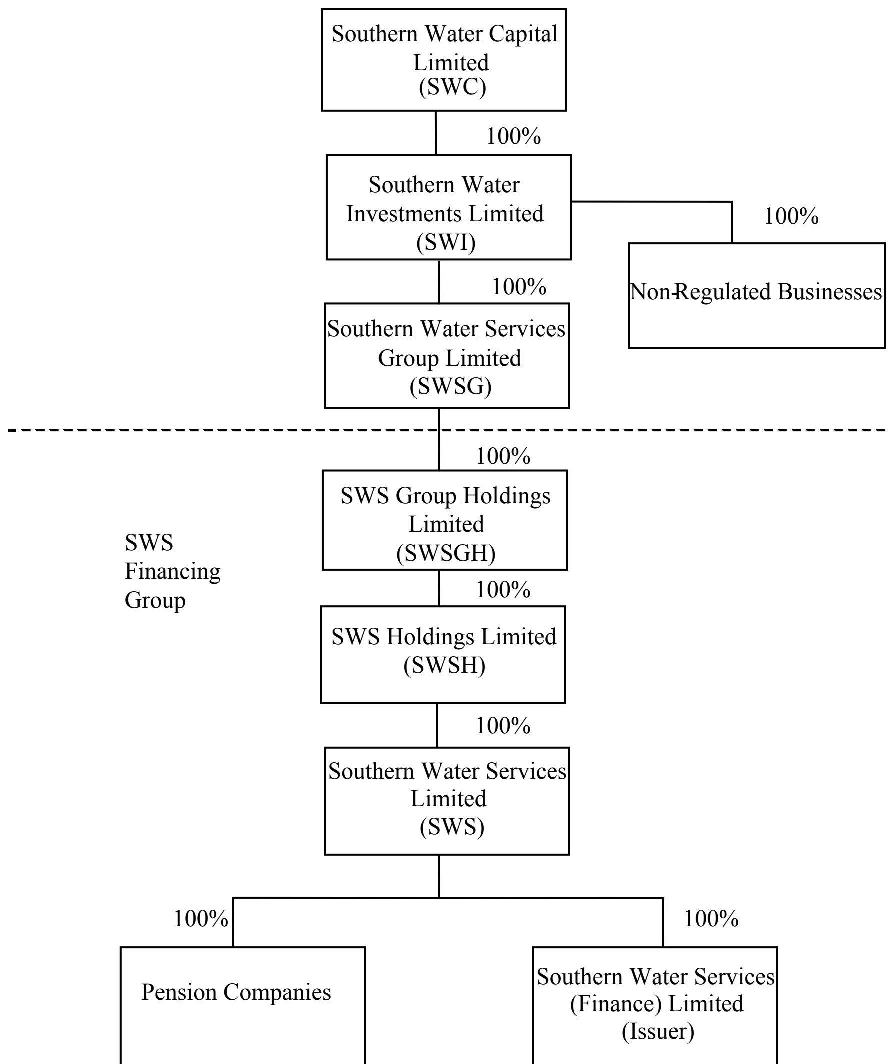


Figure 1 illustrates the ownership structure of the SWS Financing Group:

Figure 1 provides an overview of the ownership structure of the SWS Financing Group as follows:

- The Pension Companies and the Issuer are wholly owned subsidiaries of SWS.
- The entire issued ordinary share capital of SWS is held by SWSH, whose entire issued share capital is held by SWSGH.
- SWSGH is a wholly owned subsidiary of Southern Water Services Group Limited ("**SWSG**"), which is a wholly owned subsidiary of SWI.
- SWI is a wholly-owned subsidiary of Southern Water Capital Limited ("**SWC**").
- The largest shareholder in SWC is Royal Bank Investments Limited, a subsidiary of The Royal Bank of Scotland plc.
- Each of SWSGH and SWSH is a special purpose vehicle incorporated to be the holding company of SWS and the Issuer and (in the case of SWSGH) SWSH, to enter into the Finance Documents and in particular to grant security over the shares of its respective subsidiary pursuant to the Security Agreement.

FIGURE 2 – PROGRAMME STRUCTURE

SWC
SWI
SWSG
SWSGH
SWSH
SWS
Issuer
Customer Revenues
Class A1 Preference Shares and Class B Preference Shares
Class A2 Preference Shares
SWS/ SWSG Loan
Guarantee and Security
Guarantee and Security
Guarantee and Security
Security Trustee
Finance Lessors
Finance Leases
Other Authorised Credit Facility Providers[2]
Principal and Interest
Issuer/SWS Loan Agreement
Guarantee and Security
Bond Proceeds
Bondholders/ Bond Trustee
Authorised Credit Facilites (1)
Principal and Interest
DSR Liquidity Facility
Fianncial Guarantee Fee
Fianncial Guarantee
Hedging Agreements
O & M Reserve Facility
Senior and Junior Mezzanine Facilities
Hedge Counterparties
O & M Reserve Facility Providers
DSR Liquidity Facility Providers
Senior and Junior Mezzanine Facility Providers
Fianncial Guarantors of Wrapped Bonds
Security Trust and Intercreditor Deed

Note:

1 Including Initial RCF Facility, Initial Term Facility, Second Artesian Term Facility and Second Revolving Credit Facility

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

- The Issuer may under the Programme issue Class A Wrapped Bonds (guaranteed as to scheduled principal and interest by a Financial Guarantor), Class A Unwrapped Bonds, Class B Wrapped Bonds (guaranteed as to scheduled principal and interest by a Financial Guarantor) and Class B Unwrapped Bonds. On the Initial Issue Date, the Issuer issued the Series 1 Bonds and on the Third Issue Date the Issuer issued the Series 2 Bonds.

- The Issuer and/or SWS may also borrow money from Authorised Credit Providers under Authorised Credit Facilities for funding the working capital and capital expenditure requirements of SWS, to service and repay the SWS Financing Group's indebtedness and for the SWS Financing Group's general corporate purposes. On the Initial Issue Date, the Issuer entered into the Initial RCF Facility Agreement and also borrowed the Initial Term Facility. In July 2004, Artesian advanced the Second Artesian Term Facility to the Issuer. In June 2005, SWS entered into the Second Revolving Credit Facility Agreement. See Chapter 7 ("*Summary of the Financing Agreements*") under ("*Additional Resources Available – Initial Authorised Credit Facilities*").

- The Issuer may additionally borrow money from O&M Reserve Facility Providers under O&M Reserve Facility Agreements for funding the operating and maintenance expenditure of SWS.

- The Issuer, on the Initial Issue Date, borrowed the Senior Mezzanine Facility and the Junior Mezzanine Facility from the Initial Mezzanine Facility Providers. SWC is now the sole Mezzanine Facility Provider.

- SWS issued the Class A1 Preference Shares and the Class B Preference Shares to Veolia Water Investment Limited and to syndicatees nominated by it and the Class A2 Preference Shares to SWI on the Initial Issue Date. The Class A1 Preference Shares and the Class B Preference Shares were subsequently acquired by SWC.

- Finance Lessors may provide financing of equipment to SWS.

- The terms under which the Issuer and/or SWS may incur financial indebtedness, including issuing Bonds under the Programme, are set out in the CTA.

- The Issuer may on-lend to SWS the proceeds of each Series of Bonds and each advance to the Issuer under each Authorised Credit Facility (other than any DSR Liquidity Facility – see below), pursuant to Issuer/SWS Loan Agreements. All indebtedness owing by SWS to the Issuer under each Issuer/SWS Loan Agreement will reflect the corresponding amount and terms of borrowing by the Issuer under the relevant Sub-Class of Bonds or the relevant Authorised Credit Facility or, where such borrowing is hedged under a Hedging Agreement, the notional amount and terms of such Hedging Agreement. Repayment by SWS of this indebtedness to the Issuer is capable of producing funds to

service any payments due and payable on the Bonds and any relevant Authorised Credit Facilities.

- The Issuer is required to hedge its interest rate and currency exposure under the Bonds by entering into interest and currency swap agreements and other hedging arrangements with Hedge Counterparties in accordance with an agreed hedging policy. The economic effect of the hedging will be passed on to SWS through the relevant Issuer/SWS Loan Agreement.

- The Issuer's obligations to repay principal and pay interest on the Bonds and the Mezzanine Debt and under each Authorised Credit Facility to which it is party as borrower are intended to be met primarily from the payments of principal and interest received from SWS under the Issuer/SWS Loan Agreements. The Initial Issuer/SWS Loan Agreement, the Second Issuer/SWS Loan Agreement and the Third Issuer/SWS Loan Agreement provide, and each other Issuer/SWS Loan Agreement will provide, for payments to become due from SWS to the Issuer on dates and in amounts that match the obligations of the Issuer to its various financiers under its financial arrangements plus a small profit margin.

- The Issuer may draw under any DSR Liquidity Facility provided to meet any shortfall in the amounts available to it to meet interest payments on the Class A Bonds and the Class B Bonds and certain other payments ranking in priority to or *pari passu* with the Class A Bonds and Class B Bonds of such Series (excluding any principal repayments on Class A Bonds and any principal repayments and Subordinated Coupon Amounts on Class B Bonds).

- The respective obligations of SWS and the Issuer to its Secured Creditors are guaranteed by each other in favour of the Security Trustee. SWSH and SWSGH in turn guarantee in favour of the Security Trustee the respective obligations of SWS and the Issuer and the obligations of each other.

- The obligations of each of SWS, the Issuer, SWSH and SWSGH are secured in favour of the Security Trustee under the terms of the Security Agreement.

- The guarantees and security granted by the Obligors are held by the Security Trustee for itself and on behalf of the Secured Creditors under the terms of the STID, which regulates the rights and claims of the Secured Creditors against the Obligors and the duties and discretions of the Security Trustee.

CHAPTER 4
DESCRIPTION OF THE SWS FINANCING GROUP

Introduction

SWS took over its functions as a successor to the former Southern Water Authority in respect of water supply and wastewater services on 1 September 1989 and its principal activity is the provision of water and wastewater services.

It operates under a licence which has a 25 year notice period (see Chapter 6 "*Water Regulation*" under "*Termination of a licence*"). The main provisions of the Licence are described in Chapter 6 "*Water Regulation*" under "*Licences*".

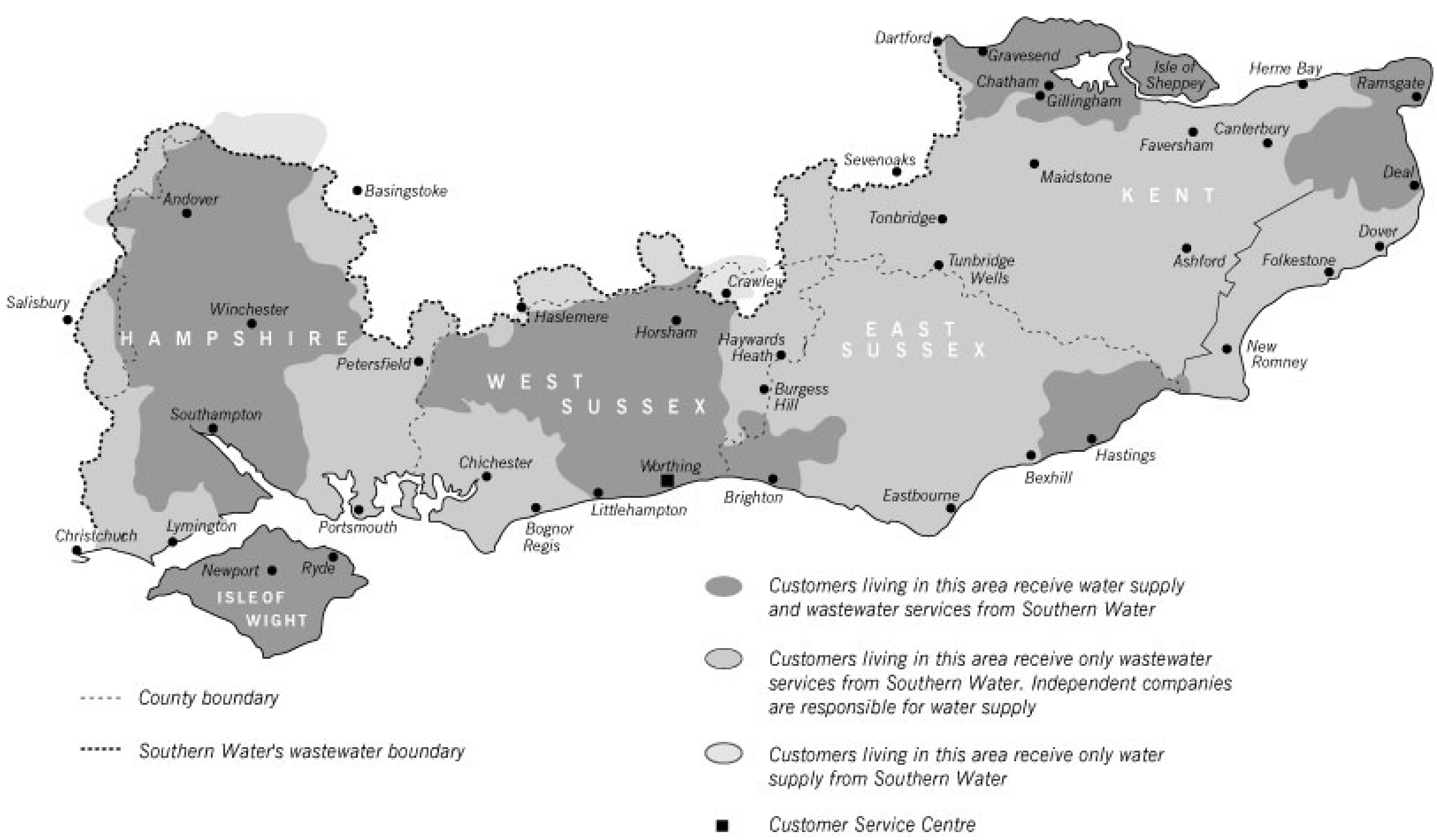
A copy of the Licence can be viewed on Ofwat's website (www.ofwat.gov.uk).

SWS is the eighth largest water and wastewater services company in England and Wales, based on turnover (source: Financial Performance and Expenditure of the Water Companies in England and Wales 2004-2005 Report; Ofwat, September 2005).

For the year ending 31 March 2006, SWS had a pre-tax net profit of £94 million on turnover of £542 million. In the year ended 31 March 2006, SWS employed an average of approximately 1,901 full time, part time and agency staff. SWS' RCV was £2,519 million as at 31 March 2006.

SWS was incorporated under the Companies Act 1985 and registered in England and Wales on 1 April 1989 with limited liability under number 02366670. The registered office of SWS is Southern House, Yeoman Road, Worthing, West Sussex BN13 3NX. SWS is a wholly-owned direct subsidiary of SWS Holdings Limited and its authorised share capital is £46,050,000 divided into 46,050,000 ordinary shares. 56,000 ordinary shares have been issued of which all have been fully paid up. The only subsidiaries of SWS are the Issuer and the Pension Companies.

The Area Served



SWS operates in an area of approximately 10,550 km^2 in the counties of Kent, East and West Sussex, Hampshire and the Isle of Wight, and small parts of Wiltshire, Berkshire and Surrey (the "**Region**").

Regulation

SWS is principally regulated under the provisions of the WIA. The Secretary of State for Environment, Food and Rural Affairs (the "**Secretary of State**") and the Water Services Regulation Authority ("**WSRA**") are the principal regulators of SWS. (See Chapter 6 "*Water Regulation*" for details on the regulation of Regulated Companies (as defined therein) including SWS).

SWS' area of appointment can be varied in certain circumstances by way of, for example, a so-called "inset" appointment (see Chapter 6 "*Water Regulation*" under "*Termination of a licence*"). Currently, the only inset appointment in SWS' original area of appointment is in respect of Tidworth Army Camp ("**Tidworth**"), which is on the boundaries of both SWS' and Wessex Water Services Limited's areas of appointment. Operation of Tidworth's water supply and wastewater services, previously undertaken by the Ministry of Defence, was put out to tender in 1996 and the tender was won by Thames Water Utilities Limited, which continues to supply such water and wastewater services.

As part of the remedies required by the Secretary of State following the acquisition by SWI of SWS and the Issuer, SWS was required to consent to a licence modification requiring the provision of a separate set of information in respect of the Hampshire and the Isle of Wight water supply areas. On 20 October 2003 Ofwat published a modification to Condition M of SWS' Licence which requires SWS to provide extra information to Ofwat on the water services that it supplies to the Hampshire and Isle of Wight water supply areas. This includes the condition of SWS' assets, its capital and operating costs and the reliability of water supplies.

Water Supply

Water Supply - Approximate Base Statistics 2005/06

Description	Value
Population served	2.3m
Properties served	1.03m
Domestic premises	964,160
Business/non-domestic premises	69,600
Length of mains	13,523km
Number of water treatment works	94
Number of main reservoirs	
Number of dams and impounding reservoirs	4
Number of service reservoirs	232
Average daily supply (million litres)	582
from groundwater	67%
from surface water	33%

Of the average supply of 582 million litres of water per day during the year 1 April 2005 to 31 March 2006, approximately 72 per cent. was supplied for domestic use and approximately 28 per cent. was supplied for non-domestic and industrial use.

In addition, SWS supplied approximately 22 million litres of water a day in aggregate (representing approximately 4 per cent. of the total water supplied by SWS) to South East Water, Wessex Water, Folkestone & Dover Water and Mid Kent Water under bulk supply agreements. This includes some 9.62 million litres a day supplied to Mid Kent Water from Burham Water supply works as part of the River Medway Scheme and 6.88 million litres of water a day to Mid Kent Water pursuant to the Belmont Scheme (comprising three boreholes owned and operated by SWS within Mid Kent Water's appointed area and associated pipelines). By a long-standing arrangement, Mid Kent Water inputs water abstracted from two of its sources into the Eastling Main pipeline for transfer to another of its water supply works. Approximately 0.01 million litres per day of treated water was received from Sutton and East Surrey Water and Folkestone and Dover Water pursuant to bulk supply agreements.

In September 2004, SWS completed a bulk supply arrangement with Portsmouth Water ("**Portsmouth**") for SWS to be supplied with treated water to meet peak summer demands in the Sussex North area (the "**Portsmouth Scheme**"). The Portsmouth Scheme provides for the transfer of up to 15 million litres a day from the boundary of Portsmouth's supply area to SWS' Hardham water supply works via a 10.5 km pipeline constructed in the K3 Period.

As of 31 March 2006, SWS supplied water to 61 large users (customers with annual water consumption in excess of 50 million litres) which, in the 12 month period to 31 March 2006, accounted for approximately 5.2 per cent. of the total volume of water supplied. SWS could potentially be subject to competition in respect of these customers (see Chapter 6 "*Water Regulation*").

As at 31 March 2006, approximately 277,000 households, or approximately 30 per cent. of total households supplied by SWS, had their water measured by meters, compared with 9.6 per cent. of household customers in 1992/93.

Water is treated at 94 water treatment works and is distributed to approximately 1,040,000 premises through a network of approximately 13,523 km of water mains. SWS treats water from 113 sources in the region with approximately 67 per cent. of water supplied coming from groundwater sources (predominantly chalk), approximately 28 per cent. coming from rivers, and the remaining approximately 5 per cent. being abstracted from reservoirs.

At five of the six water treatment works supplied by river sources, underground sources or bankside storage facilities can be utilised to help provide continuity of supply if the river intake is closed due to a temporary pollution hazard.

A central part of the water resources network in Kent and the eastern part of Sussex is the River Medway Scheme, incorporating the Bewl Water Reservoir, originating from a 1968 Private Act of Parliament and a subsequent agreement between SWS and Mid Kent Water. Under this scheme, Mid Kent Water is entitled to 25 per cent. of the yield of water from this reservoir.

SWS owns, operates and maintains 367 water-pumping stations, as well as 4 impounding reservoirs which have a total storage capacity of approximately 42,390 million litres, the largest, Bewl Water Reservoir (Kent), having a gross storage capacity of 31,000 million litres.

In the 12 month period ending 31 March 2006, approximately 93 million litres per day were estimated to be lost through leakage. About 82 per cent. of this leakage is estimated to be from SWS' pipes and the remainder from pipes owned by households and businesses. SWS narrowly missed its annual leakage target for the year ending 31 March 2006 but it achieved its rolling three-year average leakage target of 92 million litres per day for the three-year period ending 31 March 2006 set by Ofwat. In the year ending 31 March 2006, SWS had the lowest leakage rate of the ten water and sewerage companies (source: Ofwat press notice PN 22/06 and table of leakage data for 2005-06 by individual water company dated 21 July 2006). The leakage target for the year ending 31 March 2007 remains 92 million litres per day.

In line with industry norms, most of SWS' mains are constructed of iron, asbestos cement and plastics, with iron being the most common material.

In accordance with the 2004 Periodic Review, SWS plans that of its approximately 13,523 km of mains, 145 km (or 1.1 per cent.) will be renewed in the period 2005-2010 to maintain Ofwat "stable" serviceability.

Since 1990/91, the amount of water put into supply by SWS has decreased by approximately 18 per cent. However, SWS forecasts that the total volume of water put into supply will increase by approximately 2.5Ml/d per annum in the period 2005 to 2010 as a consequence of an underlying increase in domestic consumption and as a result of new connections to new housing developments.

During the current Periodic Review Period, SWS has agreed a £292 million investment programme with Ofwat (2005/6 prices). The principal investment targets relating to SWS water services include £111 million for the maintenance of water treatment works, reservoirs and pumping stations, £106 million in maintaining the water distribution system, £15 million in drinking water quality improvements and £60 million on water resources and meeting the needs of new housing development and growth.

SWS has developed a water resources strategy (the "**SWS Water Resources Strategy**") for the next 25 years, which was audited by W.S. Atkins Consultants Ltd., an Ofwat reporter, and submitted for approval to Ofwat and the EA. The plan developed by SWS in order to achieve this strategy is updated every year and submitted to the EA and Ofwat. It includes details of levels of service, population and housing estimates, per capita consumption, water efficiency initiatives, leakage and metering. It also gives details of SWS' position with regard to the supply/demand balance and the proposed capital programme to ensure future demands are met, as well as providing key data relating to issues such as climate change and catchment abstraction management strategies for the future.

In parallel with the SWS Water Resources Strategy, SWS has, together with the water only companies in the South East of England, developed a joint water resources strategy for the South

East of England as a whole. This takes the form of a cooperative, non-binding strategy subscribed to by the relevant Regulated Companies and endorsed by Ofwat and the EA.

SWS plans a number of investment schemes within the context of the SWS Water Resources Strategy, including:

- Upgrading the treatment process at Beauport Water Supply Works, Hastings, by 2008;
- Installing a treatment plant to remove nitrate at Luton Water Supply Works, Chatham by 2008 to ensure the final water leaving the works complies with water quality regulations;
- Constructing a pumping station at Tenants Hill, Worthing by 2008 to allow more water from the Sussex Coast resource zone to be pumped to the Sussex North resource zone in times of peak demand;
- Upgrading the peak output of Sandown Water Supply Works, Isle of Wight by 2009 to help meet peak summer demands on the Isle of Wight;
- Refurbishing Weir Wood Reservoir, East Grinstead by 2009 to help meet peak demands in the Sussex North water resource zone;
- Refurbishing Northbrook Water Supply Works, Worthing, treatment facilities by 2006 so that contaminants in the groundwater aquifer can be removed, allowing the water to be pumped into supply; and
- Refurbishment of filters at Findon Water Supply Works, Worthing, by 2006 to enable more water to be abstracted from the source.

Network enhancement and reinforcement schemes are also planned. Schemes include:

- Duplicating the existing water main from Testwood Water Supply Works in Hampshire to Rownhams service reservoir by 2007 to allow more water to be pumped to the reservoir;
- Duplicating the existing trunk water main from Hardham Water Supply Works to Itchingfield, Sussex, by 2008 to help meet peak demands; and
- Developing new trunk and distribution main systems in Swale, Kent, by 2009 to meet future demands arising from major new housing and commercial developments planned for the area.

Investigations into increasing the capacity at Bewl Water Reservoir, to meet future demand in Kent, will take place over the K4 Period. They include detailed investigations into the civil engineering, environmental and social impacts of raising the reservoir level and will be completed by 2009. The findings will be used to decide whether to proceed with this or an

alternative scheme in the K5 Period. Similar investigations are being undertaken into the development of a new source in Sussex to meet future demands in the Sussex North resource area.

SWS also plans to undertake several more general water resource investigations including further development of demand forecasts, enhancing drought plans and technical and environmental assessment of water resource development options.

As part of the SWS Water Resources Strategy, in Sussex, SWS has adopted a policy that will require the installation of a meter in residential properties when a change of owner-occupier occurs. Under this scheme, SWS plans to install approximately 60,000 meters during the K4 Period.

Surface and groundwater sources rely on rainfall over the winter period, predominantly from November to March to recharge water stocks needed for the following summer. The south of England is currently experiencing the worst drought since the 1930s. Two consecutive dry winters have left water resources significantly below normal levels and hosepipe and sprinkler bans have been implemented. SWS has taken steps to move water around its regional supply grid, from areas of surplus to areas of drought and is developing additional resources to help alleviate the situation. On 23 March 2006, SWS applied for a drought order under section 73 of the Water Resources Act 1991 to introduce further restrictions on non-essential use of water for household and/or business customers in 2006. This is to conserve essential supplies during 2006. A public inquiry into the drought order was held in April 2006 and the order was granted by the Secretary of State on 25 May 2006 for six months. SWS has not implemented the order due to recent rainfall and customer response in reducing demands but the situation is under constant review and further restrictions on usage may still be required later in the year.

Under Condition Q of SWS' Instrument of Appointment, where a supply of water is interrupted or cut off under the authority of a drought order, SWS could have to make a payment or credit the customer's account. For a household customer, the amount would be £10 for each day during which (or during part of which) the supply is interrupted or cut off, subject to the total amount not exceeding the average amount of water charges payable to SWS by household customers for the preceding charging year. For a business customer, the amount would be £50 for each day during which (or during part of which) the supply is interrupted or cut off, subject to the total amount not exceeding the amount of water charges payable by that customer for the supply of water to those premises for the preceding charging year or, if the customer was not liable to pay those charges, £500. The maximum aggregate amounts payable by SWS for a period of interruption or cut off in such circumstances could be Sussex North £15 million, Sussex Coast £31 million, Sussex East £7 million, Kent Medway £24 million and Kent Thanet £12 million. SWS would not be liable to make any payments under this Condition Q where the circumstances were so exceptional that it would have been unreasonable to have expected the interruption or cut-off to have been avoided. The amount of rainfall during the winter 2006/07 will be of critical importance to water resources available to supply in 2007.

All water supplied is treated at water supply works before distribution. Water quality is monitored by SWS through a programme of regular sampling and analysis. Sampling of water supplies is carried out in accordance with the Water Supply (Water Quality) Regulations 2000

which sets out the number of samples to be taken depending on the volume of water produced or the population served.

SWS operates a quality assurance system approved to British Standards Institution ("BSI") standard ISO 9002. SWS has approved procedures for the production of water up to the supply point from service reservoirs. These are used to monitor the daily activities which control water quality. These procedures are audited by the BSI on a six monthly basis.

Wastewater Services

Wastewater - Approximate Base Statistics 2005/06

Description	Value
Population served	4.25m
Properties served	1.78m
Domestic	1,683,500
Business/non-domestic premises	98,000
Length of sewers	21,397km
Number of wastewater treatment works	367
Number of coastal outfalls/marine treatment works	3
Sewage sludge disposal:	
% vol. sludge discharged agriculture	94.3
% vol. sludge discharged landfill	5.7
Number of sewerage pumping stations	2,196
Volume of wastewater treated daily	1,300Mld

SWS provides wastewater services to approximately 4.25 million people in Kent, Sussex, Hampshire and the Isle of Wight (the "**Wastewater Region**"). SWS collects and treats approximately 1,300 million litres of wastewater every day via approximately 21,397km of sewers. Approximately one half of the population in SWS' appointed area resides in urban areas along an extensive coastline. Accordingly, the majority of SWS' sewage discharge is into estuarial or coastal waters. This includes an average volume of 26.56 million litres per day of trade effluent from approximately 1,153 industrial customers, who have permission to discharge trade effluent, subject to specific controls. These figures exclude storm flows and include any infiltration. A number of factors, including rainfall, may cause flows within SWS' wastewater network to vary from time to time. In particular, an influx of visitors into the Wastewater Region during the summer holiday period contributes to an increase in the sewage flow.

As at 31 March 2006, SWS owned, operated and maintained 367 sewage treatment works, three coastal outfalls/marine treatment works and approximately 21,397 kilometres of sewers receiving foul and surface water through a mixture of combined (foul and surface water), separate and partially separate drainage systems. There are 2,196 sewage pumping stations within the Wastewater Region, which form an integral part of the wastewater system.

SWS estimates that approximately 92 per cent. of the wastewater received by it is treated, with the remainder discharged through sea outfalls.

The wastewater system has been constructed principally of clay ware, concrete, brick and iron.

SWS has identified sewers as being either “critical” or “non-critical” based on the methodology developed by the Water Research Council. At 31 March 2006, there were some 6,587 km of “critical” sewers (sewers located in places where their malfunction would cause material disruption) (constituting 30.8 per cent. of the total length of sewers) in the Wastewater Region. Over half of these “critical” sewers have been inspected by closed circuit television as part of an on-going programme to assess their structural condition. In accordance with the 2004 Periodic Review, SWS plans that 56.1 km (or 0.9 per cent. of the total) of “critical” sewers will be renewed or renovated during 2005-2010. At least 113.2 km (or 0.8 per cent. of the total) of “non-critical” sewers are planned to be replaced or renovated over the same period.

Investment in maintaining sewage treatment works has gradually increased over the last ten years. However, despite this increased expenditure, monitoring demonstrates that overall performance has yet to stabilise and it is SWS’ intention to return to previously achieved performance levels. Site inspections and modelling techniques demonstrate that the desired improvement can only be achieved by significantly increasing the level of replacement and refurbishment of SWS’ assets. SWS intends to refurbish 97 treatment works during 2005 – 2010. Ofwat recognised this in the 2004 Periodic Review and increased the provision for investment in this area. The level of refurbishment of each treatment works will vary from replacing end of life assets, plant and equipment through to providing additional treatment capacity. The performance of this group of assets is determined by Ofwat using various measures and is currently reported as “deteriorating”. It is SWS’ intention to achieve a “stable” determination by 2007/08. The current performance of many of the treatment works is affected by quality failures relating to the concentration of metals in the effluent. Typically, these metals are from industrial sources within the sewerage catchments.

SWS’ strategy for sludge disposal is based on environmental factors, planning constraints, the volume of sludge and the unit cost of disposal. The majority of treated sludge is recycled for use as a fertiliser on agricultural land. The recycling of sludge in such a manner is regulated and previous investment in sludge treatment ensures that the strict standards are met. This environmentally sustainable recycling route negates the need for other disposal methods such as incineration.

In the 2005 bathing season the EA tested 79 designated bathing waters in SWS’ Wastewater Region for bacteria, physicochemical parameters, and the presence or absence of enteroviruses. In the 2005 bathing season, all beaches passed the mandatory compliance standards.

Any pollution or drinking water quality incident could result in criminal prosecution leading to the imposition of fines on SWS, civil liability in damages to third parties and/or requirements to clean up or otherwise deal with the effects of contamination and/or operational requirements to upgrade plant and equipment.

During the current Periodic Review Period SWS has agreed a £1,405 million (2005/6 prices) investment programme with the WSRA. The principal investment targets relating to SWS sewerage services include £487 million for the maintenance of sewage treatment works and pumping stations, £79 million in maintaining the sewer system, £683 million towards

environmental quality improvements defined by the Environment Agency, £62 million to meet demands from growth and new housing development and £94 million to reduce flooding from sewers.

Rates and Billings

Water supply and wastewater services are charged separately and, therefore, charges are set (within the overall level set by Ofwat) so as to reflect the average costs of providing each service for each class of customers. Each year, SWS submits a pricing structure to Ofwat (within the overall limit set by Ofwat) for approval by Ofwat. The average SWS household bill for water supply and wastewater services for the 2006/07 year is £313, comprising £112 for water supply and £201 for wastewater services. During the year ended 31 March 2006, approximately 65 per cent. of turnover in respect of water and wastewater customers relates to supplies to unmetered customers, and approximately 35 per cent. to customers who pay by meter.

Charges for customers with unmetered water supplies are based on the rateable value of their premises, together with a standing charge, for both water supply and wastewater services. Charges are billed in advance on an annual basis with payment annually, half-yearly or (with the agreement of SWS) by instalments.

Charges for customers with metered water supplies are based on the measured volume of water supplied, together with a standing charge generally according to the size of the meter, for both water supply and wastewater services. Wastewater charges include a fixed or assessed allowance against volume to reflect water supplied that is not discharged to a sewer. Charges for small meters are billed half-yearly, and more frequently for larger meters.

SWS' contracts with customers are governed by English law.

No direct charge can be made to highway authorities for highway drainage connected to wastewater infrastructure, the cost of which is recovered through wastewater charges to customers as a whole.

Domestic Customers

Most domestic customers are unmetered. Although the domestic rating system was discontinued in 1990 (under the provisions of the UK Local Government Finance Act 1988), water companies were originally allowed to continue to use rateable values (as at 31 March 1990) for charging until 1 April 2000 under the WIA. More recently, following a review of water and wastewater charges in England and Wales, the UK Government decided to allow companies to continue using the system after that date. At the same time it proposed changes designed to encourage the use of meters for domestic properties.

Certain changes have been implemented by the Water Industry Act 1999 (the "**WIA 99**") which grants domestic customers the right:

- to resist water metering in their current homes where they are not using water for non-essential purposes (such as swimming pools and sprinklers);

- to have a free meter installed if they wish to have one, where this is practicable; and

- where they have taken up the right to have a free meter installed, to revert to an unmetered basis of charging within 12 months if they so choose.

In addition, provisions of the WIA, as amended by the WIA 99, serve to:

- prevent disconnection of domestic customers and other protected premises for non-payment;

- empower the Secretary of State to make provisions which protect vulnerable customers with high essential water use, who live in homes with meters, from higher than average bills; and

- prevent charges schemes from taking effect until approved by Ofwat and give Ofwat a duty to take into account guidance from the Secretary of State.

In calculating the wastewater charges of metered domestic customers, the volume of clean water supplied is used as the basis of the charge less a fixed allowance of 7.5 per cent. of such volume made in respect of water not discharged to a sewer (for example, water used outside the home for garden watering and washing cars).

Non-domestic customers

Most industrial and other non-domestic supplies are metered. In calculating the wastewater charges of industrial and commercial metered customers, the volume of clean water supplied is used as the basis of the charge less a fixed allowance of 5 per cent. of such volume made in respect of water not discharged to a sewer. Certain industrial and commercial metered customers receive a higher allowance where a significantly higher volume of water supplied is not discharged to a sewer. Trade effluent is normally charged separately on a formula basis taking account of the volume of effluent, its strength and costs of removal and treatment.

Collections

SWS' collection methods include full payment or instalments using direct debit, banks, the internet, post office, PayPoint or direct payment to SWS, through to doorstep collections and recourse to court procedures in appropriate circumstances. Disconnection of domestic customers from the water supply network for failure to pay charges is prohibited following the introduction of the WIA 99. In the light of this, SWS has reviewed the underlying collections risk of its receivables and, accordingly, its bad debt charge for the year ended 31 March 2006 is £12.9 million. Industrial and commercial customers are subject to a range of actions, including disconnection and court proceedings where failure to settle charges occurs.

Revenue Deviations from Ofwat's Projections

In general, SWS is not protected, in respect of each Periodic Review Period, against decreased revenue arising from any revenue deviations during that Periodic Review Period from Ofwat's

projections for such Periodic Review Period, including demographic changes affecting SWS' customer base, the loss of a major customer, unexpected reductions in customers or reduction in volumes consumed or discharged by customers, and loss of business through inset appointments.

Accordingly, at Periodic Reviews Ofwat factors into its projections assumptions about numbers of customers and volumes consumed or discharged. Until the following Periodic Review, SWS bears the risk that actual numbers of customers and volumes consumed or discharged will fall short of the assumptions reflected in the RPI+K price cap but will equally get the benefit of any out-performance. Since actual out-turn revenues are used as the basis for the setting of price limits in the subsequent five year period, any deviation from revenue projections in the previous five year period may be reflected in such price limits.

In certain circumstances, SWS may apply for an IDOK as described in Chapter 6 "*Water Regulation*" under "*Interim Determinations of K*".

Capital Investment Programme

The Ofwat Final Determination for the five year period starting on 1 April 2005 (the "**K4 Period**") sets out a level of investment for capital projects (both new projects and asset maintenance) of £1,697 million (at 2005/6 prices). This amount has been taken into account by Ofwat in determining SWS' RCV over the course of the K4 Period, and SWS will be permitted to recover in respect of such amount through customer charges its depreciation costs and an allowed return intended to compensate it for financing costs and provide a permitted return of capital. Ofwat also defines the obligations associated with that investment and sets out target implementation dates. Approximately £1,405 million of this expenditure relates to wastewater services, with the balance relating to water supply projects.

The following table summarises the levels of capital expenditure over the period 2005 to 2010 as set by Ofwat.

	Capital expenditure (net)		
	Five-year total		
Expenditure (£m)	**Water**	**Sewerage**	**Total**
Base service — Infrastructure renewals expenditure	106	79	185
Base service — Non-infrastructure capital maintenance	111	487	598
Supply/demand balance	60	62	212
Quality enhancements	15	683	698
Enhanced service levels	0	94	94
Total	**292**	**1,405**	**1,697**
£ per property per year	58	154	212

SWS' capital programme is the fourth largest in the industry. The two significant categories of construction works contracts under which work is being performed pursuant to the Final Determination for the K4 Period are the Single Entity Contract and the Utility Service Contracts (each as defined below).

The "**Single Entity Contract**" is the contract under which SWS outsources some of its key capital investment programme work to 4Delivery Limited ("**4D**"), a joint venture vehicle owned by United Utilities (40 per cent.), Costain (40 per cent.) and MWH (20 per cent.). Under the Single Entity Contract, 4D is required to manage, design and deliver 270 schemes, which are all stand-alone construction projects for the modification or extension of existing water mains, sewers, water supply works and wastewater treatment works. Most of the schemes have an individual value of between £1 million and £5 million each, although a small number of schemes have a value of up to £50 million. The total value of the Single Entity Contract is approximately £750 million. The pricing structure of the contract is based on reimbursable actual costs with a target cost and a maximum entitlement set at programme level. Any costs in excess of such target cost are borne by SWS and 4D on an equal basis up to the maximum entitlement. Costs above the maximum entitlement are borne by 4D up to the limit of a cap specified in the

contract. Any costs savings in delivering the schemes below the contract target cost will be shared equally between SWS and 4D.

A £30 million performance bond has been issued to SWS in respect of 4D's obligations under the Single Entity Contract. In addition, 4D's obligations under the Single Entity Contract are guaranteed by its parent companies to a total value of £57 million. The Single Entity Contract also requires further guarantees to be obtained from first tier sub-contractors up to a value of £65 million.

On 31 March 2005, the Security Trustee, acting on behalf of the Majority Creditors, granted SWS a waiver in respect of certain aspects of the Single Entity Contract described in Chapter-4 (*Description of the SWS Financing Group - Capital Investment Programme*) that do not comply with the Outsourcing Policy. The waiver protects SWS against the following non-exhaustive list of actual or potential non-compliances:

- there is no requirement in the Single Entity Contract for the parent guarantors to be rated not less than A-from S&P, A3 from Moody's or A-from Fitch or for performance bonds to be in an amount of not less than 10 per cent. of the contract value;
- the aggregate liability of the contractor under the Single Entity Contract is subject to a limit of less than the value of the Single Entity Contract;
- the Single Entity Contract might result in SWS sub-contracting, in any year, in excess of 50 per cent. of (a) its total Projected Operating Expenditure in such year and (b) its total Capital Expenditure in such year to any single Contractor.

The "**Utility Services Contracts**" or "**USC**" comprise a number of contracts for small scale utilities works (with the majority up to a maximum value of approximately £100,000 each), including construction works and also associated management activities.

The contracts, which account for approximately £400 million of the capital expenditure for the K4 period, currently include:

- Water distribution – Clancy Docwra (approximately £20 million per year). Under the relevant USC, pipelaying and construction activities previously carried out by SWS have been outsourced.
- Sewerage – Holleran, Mouchel Parkman JV (approximately £25 million per year).
- Waste management – Viridor Waste Management (approximately £13 million per year).
- Mechanical and electrical maintenance and renewals – Morrison Utility Services (approximately £35 million per year).

The mechanical and electrical contract commenced in 2003 for a period of three years with an option to extend by two years. It was extended in April 2006. The water distribution and

sewerage contracts were entered into in June 2004 for a three year period with options to extend by two years. The waste management contract commenced in August 2004 for a period of seven years.

SWS manages and controls the USC through dedicated contract management teams and retains authority for all works. To manage performance, key performance indicators have been identified and are monitored on a monthly basis.

The contractors' obligations under the water distribution and sewerage contracts are guaranteed by their respective parent companies and backed by a performance bond with a predetermined value equal to 10 per cent. of the annual value of the relevant contract.

If SWS does not incur the expenditure necessary to complete the delivery of a defined obligation during the relevant Periodic Review Period, Ofwat would be entitled to reduce SWS' RCV to reflect this. Such reduction may be implemented by Ofwat by way of an IDOK (if the amount of expenditure which has not been incurred is material), or otherwise at the next Periodic Review. Ofwat should then include the relevant defined obligation (and associated capital expenditure) as part of its determination of the level of investment and associated defined obligations for the subsequent Periodic Review Period. In addition to any RCV reduction, Ofwat would be entitled to claw back any benefit received by SWS in the original Periodic Review Period in relation to the defined obligations which have not been fulfilled.

SWS' ability to fulfil defined obligations, and the level of associated expenditure, can be affected by circumstances and third parties (such as planning authorities) beyond SWS' control. One large scheme (in the order of £200 million) where SWS has experienced particular difficulties in obtaining planning permission is the provision of a new wastewater treatment works for discharges from Brighton and Hove to satisfy the Urban Waste Water Treatment Directive. Ofwat have made provision for the delivery of this work in the K4 Period and SWS plans delivery by March 2010. Following an extensive consultation and selection process SWS submitted a planning application to build the works at Peacehaven, East Sussex. East Sussex County Council were unable to determine the application and SWS lodged an appeal to the Secretary of State. A public inquiry commenced on 21 June 2006 for 7 weeks. The final decision on the scheme will rest with the Secretary of State. A decision is expected in the spring of 2007, once due process has been followed.

Asset Condition and Serviceability

The Licence requires SWS to produce and provide to Ofwat an Underground Asset Management Plan (the "**UAM Plan**") which, among other things, shows the expenditure necessary in each year to ensure that asset condition is maintained in an appropriate state, and tracks the condition of SWS' assets over time (in practice, Ofwat requires information in respect of both above and below ground assets).

The latest Ofwat assessment of the performance of SWS' assets shows "stable" performance for its water service and sewerage infrastructure and a "deteriorating" performance for its sewerage non-infrastructure. SWS is committed, under the monitoring plan agreed at the 2004 Periodic Review, to achieve a stable performance on all of its assets by March 2008. Ofwat has increased

the provision for expenditure in this area and SWS has made provisions in its investment plan which aim to achieve the required improvement.

Information Technology

Over the period from 1997 to 2006, SWS replaced the majority of its mainframe information technology systems. One exception is SWS' current billing system which is a business critical application based on mainframe computer technology developed in the late 1980s. SWS has entered into a contract for development of a replacement billing and customer management system for implementation in time for the March 2007 billing process.

SWS plans to invest further in new, integrated front and back office solutions to continue the enhancement of business process support and data management. Infrastructure upgrades are in progress to provide an enhanced communications backbone to support flexible working practices such as field data capture and business process outsourcing.

A number of SWS' information technology services are currently provided under contract by a mix of onshore and offshore service providers. Services include network, infrastructure, desktop and application support and project delivery management.

Property

SWS' property interests consist substantially of freehold interests, and there are estimated to be between 3,000 and 4,000 separate titles (excluding pipeline interests). As a result of the reorganisations of local government and water-related services in 1974 and privatisation of the water industry in 1989, SWS inherited many of its sites, and is not able to deduce full legal title to all of its real property. Those properties where this is true fall into the following broad categories:

- properties in respect of which SWS is believed to have legal title but does not possess full documentary evidence to prove such title (the deeds having been lost or destroyed or never provided by the previous title holder); and/or

- properties in respect of which SWS has acquired or could acquire the necessary rights by compulsory purchase, or claim prescriptive rights or adverse possession.

SWS is not involved in any ongoing disputes, in relation to title to property, of a material nature. SWS has a programme of first registration at HM Land Registry of its current unregistered titles over the next two years.

Insurance

SWS maintains insurance cover which it believes is consistent with the generally accepted practices of prudent water and sewerage undertakers, including insurance policies against property damage and business interruption, employer's liability, public liability and directors' and officers' liability.

Litigation/Actions

In common with other companies in the water and wastewater industry, SWS is frequently involved in, or is the subject of, civil and criminal proceedings, but, save as disclosed herein, SWS is not, and has not been, involved in any governmental, legal or arbitration proceedings (including any such proceedings which are pending or threatened of which SWS is aware) during the 12 months preceding the date of this Prospectus which may have or have had in the recent past significant effects on the financial position or profitability of SWS. In October 2005, SWS reported to its regulator Ofwat and to the Serious Fraud Office inconsistencies it had found between its reported and actual performance of general levels of service requirements (in relation to the handling of customer complaints). SWS and Ofwat jointly instructed KPMG LLP to investigate the irregularities and those investigations are not yet concluded. The Serious Fraud Office has been kept informed about the investigations and has announced that it is to undertake its own investigation. SWS has undertaken to Ofwat that it will pay in full any amounts found to be due to identified customers and if the irregularities brought to light by the investigations reveal that SWS has benefited in terms of its price reviews to the detriment of its customers, it will fully adjust prices to SWS customers. The appropriate adjustment to future prices will be made by agreement with Ofwat. On 31 March 2006, Ofwat published a press notice and served notice on SWS under section 22A(4) of the WIA of its intention to impose a penalty on SWS. The notice stated that "the proposal to impose a penalty is in respect of Southern Water's failure to achieve standards of performance prescribed under sections 38(2) and 95(2) WIA, namely the GSS Regulations, at all material times between 1 April 2005 (the date on which the Director's power to impose a penalty commenced and from which the Director's power to impose a penalty may be exercised) and the date of this notice". On 7 June 2006, Ofwat served notice on SWS under section 203(2) of the WIA requiring SWS to produce documents and furnish information in relation to its misreporting of information to Ofwat in its June returns and at other times, in particular information in relation to customer services. The notice stated that "Ofwat wishes to preserve its ability to impose a penalty on Southern Water in relation to any contravention of Conditions J and/or M of Southern Water's appointment by Southern Water by reason of misreporting information to Ofwat in its June return submitted to Ofwat on 10 June 2005 and in information provided to Ofwat at other times subsequently. In addition to requesting information and documents, serving this notice now allows Ofwat to preserve its ability to impose a penalty on Southern Water in relation to such contraventions which occurred in the 12 months prior to the date of this notice". A penalty may not exceed 10 per cent. of the company's turnover (which would represent two per cent. RCV), determined in accordance with the Water Industry (Determination of Turnover for Penalties) Order 2005 (SI 2005 No. 477). The notes to the notice of 31 March 2006 state that "the 10 per cent. limit applies to each breach for which a penalty is imposed, rather than representing a cumulative limit for a financial year".

Non-Regulated Activities

SWS's non-regulated businesses are not material to the group, generating approximately £9 million annual income (being turnover and operating income) and £4.3 million operating profit for the year ending 31 March 2006. In addition SWS has a residual non-core property portfolio that is being realised over time (£5 million profit on disposals of fixed assets for the year ending 31 March 2006).

Activity	**Revenue £m**	**Operating Profit £m**
Scientific services	1.8	0.2
Land searches	2.8	1.3
Aerials	1.4	1.3
Other	3.0	1.5
Total	**9.0**	**4.3**

Management and Employees of SWS

Directors and Secretary of SWS

The SWS board consists of eight individuals.

No director has any actual or potential conflict of interest between his duties to SWS and his private interests or other duties.

The directors and secretary of SWS are set out below, each of whose business address is Southern House, Yeoman Road, Worthing, West Sussex BN13 3NX.

Chairman - Robert Thian

Robert Thian was appointed Chairman of SWS in May 2003. He is the founder and chief executive of Renex Limited, a private equity acquisition vehicle, and a director and chairman of both of Whatman Plc and Southern Water Capital Limited. He is also a director of SWI, the Issuer, SWSG and other subsidiary companies of SWI. From 1990 to 1993, Mr. Thian was group chief executive of North West Water Group Plc.

Les Dawson - Chief Executive Officer

Les Dawson was appointed Chief Executive Officer and a director of SWS in October 2005. He had previously been closely involved with SWS as a consultant since September 2004 advising on procurement and organisational structure and change. From 2000 to 2003 he was Managing Director, Service Delivery, and a main board director with the United Utilities PLC group of companies. He is a chartered gas and electrical engineer, as well as a water engineer, with 25 years experience in utilities. He is also a director of SWI, the Issuer, SWSG and other subsidiary companies of SWI.

Howard Goodbourn - Finance Director

Howard Goodbourn was appointed Finance Director of SWS in March 2004. He has spent a large part of his career in the utility sector in various finance roles, and was Treasurer and

divisional Finance Director with Powergen plc. He spent the early part of his career in corporate finance with Charterhouse Bank, having qualified as a chartered accountant with Deloitte. He is also a director of SWI, the Issuer, SWSG, SWSGH, SWSH and other subsidiary companies of SWI.

Barrie Delacour - Corporate Strategy Director

Barrie Delacour has worked for SWS for the past 31 years. He is also a director of SWSGH, SWSH, SWEPST and SWPT.

In addition, there is a SWC representative:

Donald Workman – Non-executive Director

Donald Workman was appointed a director of SWS in October 2004. He is Investment Director within the Corporate Banking and Financial Markets Division of The Royal Bank of Scotland plc and a director of Royal Bank Investments Limited and of other Royal Bank of Scotland companies. He is a director of Southern Water Capital Limited, as well as a director of SWI, the Issuer, SWSG and other subsidiary companies of SWI.

In addition, there are three independent non-executives:

David Golden – Independent Non-executive Director

David Golden was appointed a director of SWS in November 2003. He is chairman of Altrix Healthcare plc and heads the MPSL Group of companies. He was previously Contracts Director at British Nuclear Fuels plc and Director of Purchasing at North West Water Limited.

Simon MacDonagh – Independent Non-executive Director

Simon MacDonagh was appointed a director of SWS in March 2005. He is a consultant at international business law firm Lovells, where he was previously a partner.

Steven Marshall – Independent Non-executive Director

Steven Marshall was appointed a director of SWS in April 2005. He is Chairman of Delta PLC, and a director of Balfour Beatty PLC. He was previously Chairman of Queens Moat Houses PLC and group chief executive of Railtrack Group PLC.

Kevin Hall – Company Secretary

Kevin Hall is company secretary of SWS. He has worked for SWS for the past 31 years, and is also company secretary of each other member of the SWS Financing Group, SWI, SWSG and other subsidiary companies of SWI.

Pensions

Pensions for SWS employees are currently provided through two occupational pension schemes. As at 31 March 2006 there were approximately 277 SWS employees who are not members of an

occupational pension scheme. Employees on fixed term contracts are offered access to the CSP (as defined below).

The two pension schemes which operate predominantly for SWS employees are the Southern Water Pension Scheme ("**SWPS**") and a Company Stakeholder Plan ("**CSP**"). The Southern Water Executive Pension Scheme ("**SWEPS**") has been incorporated into the SWPS. As at 31 March 2006, there were 1573 active, 1542 deferred and 1537 pensioner members of SWPS and 51 members of the CSP. SWPS is a funded defined benefit arrangement. CSP is a defined contribution scheme.

Pensions management services and secretarial support are currently provided by Capita Hartshead for the SWPS and by Standard Life for the CSP.

The funding level of the SWPS equates to a combined net FRS 17 deficit of £138.0 million before deferred tax and £96.6 million after deferred tax as at 31 March 2006. The deficit has arisen mainly as a result of such factors as turbulence in the stock market, low interest rates and reduced actuarial mortality rates.

The SWPS closed to new members from 1 April 2005. SWS has made a commitment to continue the SWPS for existing members until 2010 and to increase the company's contributions until 2018 to protect the finances of the scheme. Certain terms of the schemes were changed from July 2005 when members were given the option to contribute an extra 3 per cent. of salary to continue at existing accrual rates. They were also given the option to continue to pay the current contribution rate but build up benefits at a lower rate. Other minor changes to the SWPS were made because of legislative changes under the 2004 Finance Act.

Ofwat has indicated a general willingness subject to certain conditions to take into account increases in pension contributions as allowable operating expenditure when determining K for Regulated Companies.

Ofwat recognised the need in the 2004 Periodic Review to provide for increased employer pension contributions. In the case of SWS, the allowance is £11.6 million per year which is significantly in excess of the allowances permitted by the 1999 Periodic Review. SWS and the SWPS trustees have agreed a schedule of contributions during 2005-2010 which is consistent with this annual allowance. This schedule of contributions is however subject to review by trustees at the next triennial valuation due on March 2007, which may result in an increased level of contributions. There is no assurance that the Ofwat will take a similar approach in the 2009 Price Review.

SWSGH

SWGSH is incorporated under the Companies Act 1985 and registered in England and Wales. The registered office of SWSGH is Southern House, Yeoman Road, Worthing, West Sussex, BN13 3NX. SWSGH is a wholly-owned direct subsidiary of SWSG and its authorised share capital is £101,000 divided into 101,000 ordinary shares. 100,100 ordinary shares have been issued of which all have been fully paid up. SWSGH's subsidiaries are SWSH, SWS, the Issuer, SWEPST and SWPT.

Directors and Company Secretary

The directors and company secretary of SWSGH are set out below, each of whose business address is Southern House, Yeoman Road, Worthing, West Sussex, BN13 3NX.

The Directors of SWSGH are Howard Goodbourn and Barrie Delacour. Descriptions of their principal activities outside the SWS Financing Group can be found above under "*Management and Employees of SWS – Directors and Secretary of SWS*".

No director has any actual or potential conflict of interest between his duties to SWSGH and his private interests or other duties.

Kevin Hall is company secretary of SWSGH.

SWSH

SWSH is incorporated under the Companies Act 1985 and registered in England and Wales. The registered office of SWSH is Southern House, Yeoman Road, Worthing, West Sussex, BN13 3NX. SWSH is a wholly-owned direct subsidiary of SWSGH and its authorised share capital is £101,000 divided into 101,000 ordinary shares. 100,100 ordinary shares have been issued of which all have been fully paid up. SWSH's subsidiaries are SWS, the Issuer, SWEPST and SWPT.

Directors and Company Secretary

The directors and company secretary of SWSH are set out below, each of whose business address is Southern House, Yeoman Road, Worthing, West Sussex, BN13 3NX.

The Directors of SWSH are Howard Goodbourn and Barrie Delacour. Descriptions of their principal activities outside the SWS Financing Group can be found above under "*Management and Employees of SWS – Directors and Secretary of SWS*".

No director has any actual or potential conflict of interest between his duties to SWSH and his private interests or other duties.

Kevin Hall is company secretary of SWSH.

The Issuer

The Issuer is incorporated and registered in the Cayman Islands. The registered office of the Issuer is c/o M&C Corporate Services Limited, PO Box 309GT, Ugland House, South Church Street, George Town, Grand Cayman, Cayman Islands. The Issuer is a wholly-owned direct subsidiary of SWS and has no subsidiaries. The authorised share capital is £25,000 divided into 25,000 ordinary shares of £1 each, of which 1,000 such shares are in issue and are fully paid up.

Directors and Company Secretary

The directors and company secretary of the Issuer are set out below, each of whose business address is Southern House, Yeoman Road, Worthing, West Sussex BN13 3NX.

The Directors of the Issuer are Robert Thian, Les Dawson, Donald Workman and Howard Goodbourn. Descriptions of their principal activities outside the SWS Financing Group can be found above under "*Management and Employees of SWS — Directors and Secretary of SWS*".

No director has any actual or potential conflict of interest between his duties to the Issuer and his private interests or other duties.

Kevin Hall is the company secretary of the Issuer.

CHAPTER 5
RISK FACTORS

The following is a summary of certain aspects of the Programme documentation and the activities of the SWS Financing Group about which prospective Bondholders should be aware. The occurrence of any of the events described below could have a material adverse impact on the business, financial condition or results of operations of the Issuer, SWS or the other Obligors and could lead to, among other things;

(a) *an SWS Event of Default;*

(b) *an Event of Default under the terms and conditions of the Bonds;*

(c) *non-payment of scheduled principal and/or interest in respect of the Class A Wrapped Bonds or Class B Wrapped Bonds (if, additionally, the relevant Financial Guarantor were to default on its obligations under any Financial Guarantee);*

(d) *non-payment of unguaranteed amounts under the Class A Wrapped Bonds or Class B Wrapped Bonds; and*

(e) *non-payment of amounts in respect of the Class A Unwrapped Bonds or the Class B Unwrapped Bonds.*

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

In addition, while the various structural elements described in this document are intended to lessen some of these risks for holders of the Bonds, there can be no assurance that these measures will ensure that the holders of the Bonds of any Sub-Class receive payment of interest or repayment of principal from the Issuer in respect of such Bonds, or from a Financial Guarantor in respect of the Class A Wrapped Bonds or Class B Wrapped Bonds, on a timely basis or at all.

Regulatory and Competition Considerations

The water industry is subject to extensive legal and regulatory obligations and controls, and SWS must comply with all applicable laws, regulations and regulatory standards (see Chapter 6 "*Water Regulation*"). The application of these laws, regulations and regulatory standards and the policies of the WSRA and Ofwat could have a material adverse effect on the operations and financial condition of SWS.

Although (i) the WSRA has a duty to exercise its powers in the manner that it considers is best calculated, among other things, to ensure that SWS is able to finance the proper carrying out of any of its functions and (ii) certain changes in circumstances can trigger adjustments to price

limits between periodic reviews under the interim determinations provisions of the Licence, as with any Regulated Company, no assurance can be given that the laws, regulations, regulatory standards or policies will not change in a manner that could adversely affect the operations and financial condition of SWS.

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

Licence

Under the WIA, the conditions of the Licence may be modified by the WSRA with the consent of SWS or without SWS' 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. This outcome could also result from a merger or market investigation reference. In addition, the Secretary of State has a power to veto certain proposed modifications agreed by the WSRA and SWS. Other proposed modifications agreed by the WSRA and SWS may be vetoed if it appears to the Secretary of State that the modifications should be made, if at all, after a reference to the Competition Commission. Finally, primary legislation can create powers for the making of modifications by the WSRA without the consent of Regulated Companies. The Water Act provides Ofwat with powers to make unilateral modifications, following consultation with Regulated Companies, to give effect to the new competition arrangements and to provide for the payment of fees to cover the expenses of the new Consumer Council for Water (see also Chapter 6 "*Water Regulation*" under "*Modification of a Licence*").

Any restrictive modification to the Licence could have a material adverse impact on SWS.

A failure by SWS to comply with the conditions of its Licence, as modified from time to time, may lead to the making of an enforcement order by the WSRA or the Secretary of State which could have an adverse impact on SWS. Failure by it to comply with any enforcement order (as well as certain other defaults) may lead to the making of a Special Administration Order (as defined below). See Chapter 6 "*Water Regulation*" under "*Special Administration Orders*".

The area of appointment of SWS can also be varied in accordance with an inset appointment (see Chapter 6 "*Water Regulation*" under "*Termination of a licence*").

Termination of the Licence

Under the terms of the Licence, SWS' appointment may be terminated following the giving of notice by the Secretary of State of at least 25 years. The Licence may also be transferred from SWS at any time following the making of a Special Administration Order. The termination, non-renewal or transfer of the Licence could have a material adverse impact on SWS and, consequently, on the Issuer's ability to meet its obligations (including the payment of principal and interest) under the Bonds.

If the Secretary of State or the WSRA were to make an appointment or variation replacing SWS as the regulated water and sewerage undertaker for its currently appointed area, it would have a duty to ensure (so far as consistent with its other duties under the WIA) that the interests of SWS' creditors were not unfairly prejudiced by the terms on which the successor Regulated

Company (or Companies) replacing SWS could accept transfers of property, rights and liabilities from SWS.

So far, no compulsory licence terminations or Special Administration Orders have been made in connection with any appointed business of any Regulated Company in England and Wales. There is therefore no precedent to indicate how such processes would work in practice and the extent to which creditors' interests would be protected (see paragraphs on "*Security*" and "*Special Administration*" below).

Competition Act 1998

The Competition Act contains prohibitions relating to anti-competitive agreements and conduct and powers of investigation and enforcement (see Chapter 6 "*Water Regulation*" under "*Competition in the Water Industry*"). These powers include powers for the WSRA and Office of Fair Trading ("**OFT**") to enforce directions in order to bring an infringement to an end and to impose fines of up to 10 per cent. of worldwide group-wide turnover for the business year preceding the finding of the infringement. Also, any agreement which infringes the Competition Act may be void and unenforceable and may give rise to claims for damages from third parties.

The Water Act 2003

The Water Act 2003 received Royal Assent on 20 November 2003 and has substantially come into force. The Water Act 2003 contains a number of provisions which may affect the finances of Regulated Companies, including SWS. It contains provisions which create a new framework for competition in water supply, under which new types of "water supply licence" will be available to entrants wishing to use Regulated Companies' networks to transport water to customers (common carriage) or wishing to purchase wholesale water from undertakers for "retail" to customers. SWS may lose customers to new market entrants, and suffer reductions in revenue as a result.

However, the new market is limited to customers using in excess of 50 megalitres of water per annum. SWS estimates that it has 61 of these customers as at 31 March 2006, which accounts for 5.2 per cent. of the water services turnover.

In addition, the Water Act 2003 includes a requirement on Regulated Companies to charge entrants for common carriage and wholesale services in such a way as to recover appropriate costs.

The Water Act also includes a new power for the WSRA and the Secretary of State to impose financial penalties on a Regulated Company for contraventions of its licence, statutory or other requirements including performance standards (see also below paragraph entitled "*WSRA may impose a penalty on SWS*"). Penalties may be up to 10 per cent. of a Regulated Company's worldwide group turnover, but they must be reasonable in the circumstances of the case. Each of the above enforcement authorities is required to publish a statement of policy on the imposition of penalties, and to have regard to that statement when implementing the new provisions (see Chapter 6 "*Water Regulation*" under "*The Water Act 2003*"). Such a statement of policy with respect to financial penalties was published jointly by Ofwat, DEFRA and the National Assembly for Wales in March 2005.

Current methods for introducing or extending competition are outlined in Chapter 6 "*Water Regulation*". It is not possible to assess if, or how, such methods will affect the interests of Bondholders.

SWS Revenue and Cost Considerations

The net operating revenues generated by SWS from its water and wastewater business may not be sufficient to enable it to make full and timely payment of amounts due to creditors including under the Issuer/SWS Loan Agreements. This could have a material adverse impact on the Issuer's ability to meet its obligations (including the payment of principal and interest) under the Bonds. In addition to the regulatory and competition risks described above which could adversely affect the revenues and costs of SWS, other potential events which could result in SWS having insufficient net operating revenues to meet its financing obligations and/or the Issuer being unable to meet its obligations under the Bonds include:

Periodic Review

In carrying out a Periodic Review, the WSRA sets targets on the basis of its assessment of what constitutes an efficiently-managed Regulated Company. On that basis, prices are set so that Regulated Companies' revenues cover the cost of the "efficient" provision of operations and capital investment (as determined by the WSRA) including a company specific tax charge, and to allow a reasonable return on capital (based on an assumed opening notional gearing level of 55 per cent.). However, the WSRA is under no duty to ensure the continued solvency of a Regulated Company in all circumstances, and there is no assurance that price limits imposed by the WSRA at Periodic Reviews will permit SWS to generate sufficient revenues to enable it to Finance its functions or discharge its obligations under the Issuer/SWS Loan Agreements.

Although the methodology introduced in the 1994 Periodic Review - in particular the derivation of the "regulatory capital value" (the "**RCV**") as the measure of capital to be remunerated - was also applied with modifications in the 1999 and 2004 Periodic Reviews, the WSRA is not required to apply the same or a similar methodology in future Periodic Reviews (see Chapter 6 "*Water Regulation*" under "*Periodic reviews of K*").

As described in Chapter 6 "*Water Regulation*" under "*Interim Determinations of K*", an interim determination of price limits (an "**IDOK**") may be made between Periodic Reviews in specified circumstances, including, in the cases of SWS and most other Regulated Companies, which have the benefit of a Shipwreck Clause in the licence, the circumstances contemplated by that clause. In contrast to Periodic Reviews, the methodology to be applied for any IDOK is set out in detail in the Licence and the scope for discretion is narrower.

There is however no assurance that any IDOK sought by SWS will be made or, if an IDOK or determination pursuant to the provisions of the Shipwreck Clause is made, that any adjustment made pursuant to such an IDOK, or determination pursuant to the Shipwreck Clause, as the case may be, will provide adequate revenue compensation to SWS.

If the WSRA makes no IDOK within three months from the Regulated Company's application for such an IDOK or if the Regulated Company disputes an IDOK or a determination pursuant to the Shipwreck Clause made in relation to it by the WSRA, the Regulated Company may require

the WSRA to refer the matter to the Competition Commission for determination. Again, there is no assurance that the Competition Commission's determination of the relevant adjustment(s) will provide adequate revenue compensation to SWS.

As with a number of other Regulated Companies, the Licence does not contain a condition providing for interim adjustment to price limits to reflect variations in capital cost inflation for capital projects outside Periodic Reviews. However, Ofwat has indicated that it proposes to offer to extend this condition to all Regulated Companies' licences before the 2009 Periodic Review.

Deviations from WSRA's Projections

Under Condition B of the Licence, the RPI+K price cap limits the annual "weighted average increase" in the standard charges of SWS. This, in turn, is calculated by reference to the "tariff basket formula" (see Chapter 6 "*Water Regulation*" under "*Price Control*"), which is constructed so as to provide some compensation in respect of certain risks (for example, high rateable value customers opting for a meter). However, generally SWS is not protected, in respect of each Periodic Review Period, against revenue loss arising from any deviations during that Periodic Review Period from projections, including demographic changes affecting SWS' customer base, the loss of a major customer, unexpected reductions in customers or movements in volumes consumed/discharged by customers, and loss of business through inset appointments.

Accordingly, at Periodic Reviews, the WSRA factors into its projections assumptions relating to numbers of customers and volumes consumed/discharged. Until the following Periodic Review, SWS bears the risk that actual numbers of customers and volumes consumed/discharged will fall short of the assumptions reflected in the RPI+K price cap. Since actual out-turn revenues are used as the basis for the selling of price limits in the subsequent five year period, any deviation from revenue projections in the previous five year period may be reflected in such price limits.

Weather

SWS is at risk both from the effects of water shortages, caused by prolonged periods of drought, and from the effects of flooding.

SWS obtains a high proportion (approximately 67 per cent.) of the water which it supplies from underground sources rather than rivers and reservoirs, and inadequate winter rainfall over two or more years may prejudice the adequate recharging of such sources.

If there are supply shortfalls caused by prolonged periods of drought, additional costs may be incurred by SWS in order to provide emergency reinforcement to supplies in areas of shortage. Restrictions on water use may adversely affect revenues from metered customers and may, in very extreme circumstances (which have never been experienced by SWS), lead to significant compensation having to be paid to customers who suffer interruptions in supply. The south of England is currently experiencing the worst drought since the 1930's. Two consecutive dry winters have left water resources significantly below normal levels and hosepipe and sprinkler bans have been implemented. On 23 March 2006, SWS applied for a drought order under section 73 of the Water Resources Act 1991 to introduce further restrictions on non-essential use of water for household and/or business customers in 2006. The order was granted by the Secretary of State on 25 May 2006 for six months. SWS has not implemented the order due to recent

rainfall but the situation is under constant review and further restrictions on usage may still be required later in the year.

The amount of rainfall during the winter 2006/07 will be of critical importance to water resources available to supply in 2007. See Chapter 4 (*Description of the SWS Financing Group*) under "*Water Supply*" for further details.

The financial costs of measures taken to deal with flooding could also be significant and may adversely impact on SWS' operations and financial condition. The fact that it is not possible to forecast the occurrence of flooding makes forward planning and the making of provision for the effects of flooding difficult. Costs incurred by SWS arising from the flooding of its own property which are not fully covered by insurance, compensation to customers in relation to the effects of the inundation of the sewerage system with surface water and work undertaken to prevent reoccurrence may not be recoverable by SWS through adjustments to the price cap formula. Eastney Pumping Station, the principal pumping station draining Portsmouth, was flooded in September 2000 as a result of a storm of a severity encountered on average once every 108 years. The total damage was £2,677,000. Since this incident a number of improvements have been implemented to provide additional protection from any such future events. Due to the nature of the area served by SWS, where large areas are below sea level and there is no gravity outlet to the sea, there remains a risk of a repeat event. To minimise the risk, SWS plans to construct an additional pumping station by 2010, which will come into operation at peak flow times and also act as a standby to the existing station. Provision for this investment is included in the 2004 Periodic Review.

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

Depending on developments in case law, sewerage undertakers may in future have to negotiate contracts with the owners of watercourses in order to be able to discharge into them. The additional costs involved are expected to be significant.

WSRA may impose a penalty on SWS

In October 2005, SWS reported to its regulator Ofwat and to the Serious Fraud Office inconsistencies it had found between its reported and actual performance of general levels of service requirements (in relation to the handling of customer complaints). In response, Ofwat has served notice on SWS of its intention to impose a penalty on SWS and notice requiring further information in anticipation of a penalty. Each such penalty may not exceed 10 per cent. of the company's turnover. If such penalty is imposed (and subject to the level of such penalty), it could have an adverse effect on the ability of SWS to meet its financing obligations. (see Chapter 4 "*Description of the SWS Financing Group*" under "*Litigation/Actions*" for further detail).

Certain Legal Considerations

Security

A Regulated Company's ability to grant security over its assets and the enforcement of such security are restricted by the provisions of the WIA and its licence. For example, all licences (including SWS' Licence) restrict a Regulated Company's ability to dispose of Protected Land (as explained in Chapter 6 "*Water Regulation*" under "*Protected Land*", below). Accordingly, a licence restricts a Regulated Company's ability to create a charge or mortgage over Protected Land. In the case of SWS, the Issuer estimates that the vast majority of SWS' assets by value is tangible property which is Protected Land and cannot therefore be effectively secured. This necessarily affects the ability of SWS to create a floating charge over the whole or substantially the whole of its business. Furthermore, in any event, there is no right of a floating charge holder under the WIA to block the appointment of a Special Administrator.

The Secretary of State and the WSRA have rights under the WIA to appoint a Special Administrator in certain circumstances in respect of SWS and its business. The appointment of a Special Administrator effectively places a moratorium upon any holder of security from enforcing that security.

There are also certain legal restrictions which arise under the WIA and SWS' Licence affecting the enforcement of the security created under the Security Agreement. For example, such enforcement is prohibited unless the person enforcing the security has first given 14 days' notice to the WSRA or the Secretary of State, giving him time to petition for the appointment of a Special Administrator (see Chapter 6 "*Water Regulation*" under "*Security*").

Accordingly, the security provided over the assets of SWS in favour of the Security Trustee in respect of the Issuer's obligations under the Bonds affords significantly less protection to the Security Trustee (and, therefore, the Bondholders) than would be the case if SWS were not a Regulated Company subject to the provisions of the WIA and its Licence.

The considerations described above do not apply to the fixed and floating charges created under the Security Agreement by SWSGH, SWSH and the Issuer. The enforcement of the security granted under the Security Agreement over the shares in any company in the SWS Financing Group (other than the Issuer), including any holding company of SWS, would not be subject to the moratorium set out in the WIA nor would it be an event which would itself result in the making of the Special Administration Order. However, it is anticipated that any intended enforcement directly or indirectly of the security created by SWSH or SWSGH under the Security Agreement, to the extent that such enforcement would amount to a relevant merger situation for the purposes of the Enterprise Act 2002, would require consultation with the WSRA and would be reviewable by the OFT.

Notice of the creation of the SWS Security has not been and will not be given to SWS' customers or to SWS' contractual counterparties in respect of its contracts (other than certain material contracts). Also, any security over any amounts due from customers that constitute statutory receivables may be limited by law. In addition, if SWS were to acquire any land that was not Protected Land the charge over that land granted by the Security Agreement would take

effect in equity only. Accordingly, until any such assignment is perfected, registration effected with HM Land Registry in respect of registered land or certain other action is taken in respect of unregistered land, any such assignment or charge may be or become subject to prior equities arising (such as rights of set-off).

Special Administration

The WIA contains provisions enabling the Secretary of State or the WSRA (with the permission of the Secretary of State) to secure the general continuity of water and wastewater services by petitioning the High Court for the appointment of a Special Administrator in certain circumstances (for example, where SWS is in breach of its principal duties under its Licence or of the provisions of a final or confirmed provisional enforcement order (and in either case the breach is serious enough to make it inappropriate for SWS to continue to hold its Licence) or is unable, or is unlikely to be able, to pay its debts). In addition, a petition by a creditor of SWS to the High Court for the winding up of SWS might result in the appointment of a Special Administrator where the Court is satisfied that it would be appropriate to make such a winding-up order if the company were not a company holding an appointment under the WIA. The duties and functions of a Special Administrator differ to those of an administrator of a company which is not a Regulated Company.

During the period of the Special Administration Order, SWS has to be managed by the Special Administrator for the purposes of the order and in a manner which protects the interests of shareholders and creditors. As noted above, while the order is in force, no steps may be taken to enforce any security over the property of SWS except with the consent of the Special Administrator or the leave of the Court. A Special Administrator would be able to dispose of assets free of any floating charge existing in relation to them. On such a disposal, however, the proceeds would be treated as if subject to a floating charge which has the same priority as that afforded to the original security. A Special Administrator may not dispose of property which is the subject of a fixed charge without the agreement of the relevant creditor except under an order of the Court. On such a disposal, the Special Administrator must account for the proceeds to the chargee, although the disposal proceeds to which the chargee is entitled are determined by reference to "the best price which is reasonably available on a sale which is consistent with the purposes of the Special Administration Order" as opposed to an amount not less than "open market value", which would apply in a conventional administration for a company which is not a Regulated Company under English insolvency legislation.

Because of the statutory purposes of a Special Administration Order, it is not open to a Special Administrator to accept an offer to purchase the assets on a break-up basis in circumstances where the purchaser would be unable properly to carry out the relevant functions of a Regulated Company. The transfer is effected by a transfer scheme which the Special Administrator puts in place, subject to the approval of the Secretary of State or the WSRA on behalf of the existing Regulated Company. The transfer scheme may provide for the transfer of the property, rights and liabilities of the existing Regulated Company to the new Regulated Company(ies) and may also provide for the transfer of the existing Regulated Company's licence (with modifications as set out in the transfer scheme) to the new Regulated Company(ies). (See Chapter 6 "*Water Regulation*" under "*Special Administration Orders*").

There can be no assurance that any transfer scheme in the context of a special administration regime could be achieved on terms that would enable creditors to recover amounts due to them in full.

Insolvency Considerations: The Enterprise Act

The Enterprise Act 2002 (the "**Enterprise Act**") sets out certain reforms to corporate insolvency law, including the introduction of a prohibition on appointment of an administrative receiver in relation to companies such as the Issuer, SWSH and SWSGH.

In any event, the ability to appoint an administrative receiver to prevent an administration is unlikely to be of significance in the case of entities such as the Issuer, SWSH and SWSGH, which are subject to substantial restrictions on their activities. In addition, such ability will not be applicable in the case of SWS which is subject to the special administration regime.

Environmental Considerations

SWS' water supply and sewerage operations are subject to a number of laws and regulations relating to the protection of the environment and human health governed primarily by the DWI and the EA as described in Chapter 6 "*Water Regulation*" under "*Drinking Water and Environmental Regulation*".

It is likely that SWS and other Regulated Companies will incur significant costs in future in order to comply with requirements imposed under existing or future environmental laws and regulations (including nature conservation legislation). Although the costs arising from such changes in legal requirements (see Chapter 6 "*Water Regulation*" under "*Drinking Water and Environmental Regulation*") may, in certain cases, be eligible for the purposes of the interim determination provisions or fall to be considered as part of a Periodic Review (see Chapter 6 "*Water Regulation*" under "*Interim Determinations of K*"), there can be no certainty as to how and whether future environmental laws and regulations will impact the business and financial condition of SWS and/or the interests of the Bondholders. It is possible that Ofwat may determine that the cost of fulfilling certain obligations is likely to be less than the cost actually incurred by SWS in fulfilling such obligations. In such circumstances, the funding allowed by Ofwat may not totally cover the actual costs and SWS would bear this additional element. In practice the funding allowed by Ofwat is set for a package of obligations and some will cost more and some less.

Given the nature of SWS' operations, there is a risk that pollution or drinking water quality incidents may occur. The possible consequences of any such incident include criminal prosecution leading to the imposition of fines on SWS, civil liability in damages to third parties and/or requirements to clean up or otherwise deal with the effects of contamination and/or operational requirements to upgrade plant and equipment. The imposition of (potentially unlimited) fines, civil liability, clean-up or upgrade costs may materially and adversely affect the business and financial position of SWS. Any such incidents may also give rise to breaches of any operational environmental permits held by SWS, which could result in fines and/or termination.

In addition to environmental costs imposed upon SWS by law or regulation, SWS may be subject to additional costs resulting from public concern regarding environmental matters. For example,

farms that use sludge from SWS' sewerage operations are increasingly requiring higher levels of treatment of this sludge in response to demands from the buyers of their crops. This in turn results in higher capital and operating costs for SWS.

Catastrophe Risk

Catastrophic events such as dam bursts, fires, earthquakes, floods, droughts, terrorist attacks, diseases, plant failure or other similar events could result in personal injury, loss of life, pollution or environmental damage, severe damage to or destruction of SWS' operational assets. Any costs resulting from suspension of operations of SWS could have a material adverse effect on the ability of SWS to meet its financing obligations.

Although the Common Terms Agreement requires SWS to maintain insurance (including business interruption insurance) to protect against certain of these risks, the proceeds from such insurance may not be adequate to cover reduced revenues, increased expenses or other losses or liabilities arising from the occurrence of any of the events described above. Moreover, there can be no assurance that such insurance coverage will be available for some or all of these risks in the future at commercially reasonable rates or at all. (See Chapter 4 "*Description of the SWS Financing Group*" under "*Insurance*").

High Leverage

The SWS Financing Group has indebtedness that is substantial in relation to its shareholders equity. Taking into account retained cash reserves, such leverage of the SWS Financing Group was approximately 76 per cent. of RCV as at 31 March 2006. In addition, the Issuer has borrowings of £233.2 million under the Mezzanine Facilities and SWS has in issue Preference Shares for a consideration of £260 million, each of which are subordinated to the Class A Debt and the Class B Debt pursuant to the Intercreditor Arrangements. The ability of SWS to improve its operating performance and financial results will depend upon economic, financial, competitive, regulatory and other factors beyond its control, including fluctuations in interest rates and general economic conditions in the United Kingdom.

Accordingly, there can be no assurance as to SWS' ability to meet its financing requirements and no assurance that SWS' high degree of leverage will not have a material adverse impact on its ability to pay amounts under the Issuer/SWS Loan Agreements, which would enable the Issuer to pay amounts due and owing in respect of the Bonds. Incurrence of additional indebtedness by SWS or the Issuer, which is permitted under the Finance Documents, may materially affect the ability of SWS, the Issuer or the other Obligors to pay amounts due and owing in respect of the Bonds.

Future Financing

The SWS Financing Group will need to raise further debt from time to time in order, among other things, to:

(i) finance future capital enhancements to SWS' asset base;

(ii) on each Interest Payment Date on which principal is required to be repaid and on the maturity date of the relevant Sub-Classes of Bonds, refinance the Bonds; and

(iii) refinance any other debt (including for liquidity or working capital purposes) the terms of which have become inefficient or which have a scheduled partial or final maturity prior to the final maturity of the Bonds.

While the Common Terms Agreement and the STID contemplate the terms and conditions on, and circumstances under, which such additional indebtedness can be raised, there can be no assurance that the SWS Financing Group will be able to raise sufficient funds, or funds at a suitable interest rate, or on suitable terms, at the requisite time such that the purposes for which such financing is being raised are fulfilled, and in particular such that all amounts then due and payable on the Bonds or any other maturing indebtedness will be capable of being so paid when due.

In addition, in the 2004 Price Review, the WSRA took into account the presumed actions of a hypothetical efficiently financed company when it assessed the cost of water companies' debt. According to the WSRA, such a company would be one that retains the flexibility to respond to changing market conditions, and holds a balanced portfolio of debt. If the WSRA adopts a similar approach in subsequent Periodic Reviews, there is no guarantee that full allowance would be made for the costs of then existing fixed rate debt if current forward-looking rates at the time were lower, if the WSRA took the view that such debt had not been prudently incurred.

Issuer and Bond Considerations

Special Purpose Vehicle Issuer

The Issuer is a special purpose financing entity with no business operations other than raising the original acquisition finance for the First Aqua Acquisition, refinancing part of such financing, upon the acquisition by SWI of the Issuer, and further refinancing the same and raising external funding for SWS through the issuance of the Bonds and borrowing under the Mezzanine Facilities, the Liquidity Facilities and Authorised Credit Facilities and entering into various Hedging Agreements. Other than the proceeds of the issuance of additional Bonds, the Issuer's principal source of funds will be pursuant to the Issuer/SWS Loan Agreements and funds available to it pursuant to the Liquidity Facilities and other Authorised Credit Facilities.

Therefore, the Issuer is subject to all the risks relating to revenues and expenses to which SWS is subject. Such risks could limit funds available to SWS to enable SWS to satisfy in full and on a timely basis its obligations under the Issuer/SWS Loan Agreements and its guarantee under the Security Agreement (See "*SWS Revenue and Cost Considerations*" above).

Source of Payments to Bondholders

Although the Class A Wrapped Bonds and Class B Wrapped Bonds will have the benefit of the relevant Financial Guarantee, none of the Bonds of any Class will be obligations or responsibilities of, nor will they be guaranteed by, any of the Other Parties (other than the Guarantors and, in the case of the Wrapped Bonds, the relevant Financial Guarantor). The

guarantees by SWSGH and SWSH may be of limited value, because neither of them own, nor will own, any significant assets other than their direct or indirect shareholding in SWS.

Moreover, a Financial Guarantor will guarantee to the holders of the Class A Wrapped Bonds and holders of the Class B Wrapped Bonds only the payment of scheduled principal and interest; it will not guarantee FG Excepted Amounts.

Subordination of the Class B Bonds

Payments under the Class A Wrapped Bonds and the Class A Unwrapped Bonds (each of whatever Sub-Class) rank in priority to payments of principal and interest due on all Sub-Classes of the Class B Bonds. The Class A Wrapped Bonds and the Class A Unwrapped Bonds (each of whatever Sub-Class) rank *pari passu*.

If, on any Interest Payment Date, prior to the taking of Enforcement Action after the termination of a Standstill Period, there are insufficient funds available to the Issuer to pay accrued interest or principal on the Class B Unwrapped Bonds (after taking into account any amounts available to be drawn under any DSR Liquidity Facility or from the Debt Service Reserve Account), the Issuer's liability to pay such accrued interest will be treated as not having fallen due and will be deferred until the earliest of (i) the next following Interest Payment Date on which the Issuer has, in accordance with the Payment Priorities, sufficient funds available to pay such deferred amounts (including any interest accrued thereon); (ii) the date on which all Class A Debt has been paid in full; and (iii) an Acceleration of Liabilities (other than a Permitted Hedge Termination or a Permitted Lease Termination) and, in the case of a Permitted Share Pledge Acceleration, only to the extent that there would be sufficient funds available in accordance with the Payment Priorities to pay such deferred amounts (including accrued interest thereon). Interest will, however, accrue on such deferred amounts.

Notwithstanding the subordination of, and credit enhancement provided by, the Class B Bonds to the Class A Wrapped Bonds and Class A Unwrapped Bonds, the Issuer may, subject to certain conditions, optionally redeem some or all of the Bonds subordinated and providing credit enhancement to other Classes of Bonds.

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

Hedging Risks

The Issuer may be left exposed to interest rate risk or currency risk in the event that there is an early termination of any Hedging Agreement. A Hedging Agreement may be terminated in the circumstances set out in Chapter 7 "*Summary of the Financing Agreements*" under "*Hedging Arrangements*", including where the Hedge Counterparty is required to gross up for, or receive, payments from which tax has been required to be deducted or withheld by law, which requirement has not been able to be avoided, notwithstanding the Issuer and the Hedge Counterparty having used reasonable endeavours so to do in accordance with the relevant

Hedging Agreement. If a Hedging Agreement is terminated and the Issuer is unable to find a replacement Hedge Counterparty, then the funds available to the Issuer may be insufficient to meet fully its obligations under the Bonds, as a result of adverse fluctuations in interest rates and exchange rates or making any termination payment to the Hedge Counterparty, which payment will be in accordance with the Payments Priorities (see Chapter 7 "*Summary of the Financing Agreements*" under "*Cash Management*").

The DSR Liquidity Facilities

The DSR Liquidity Facilities and any amounts credited to the Debt Service Reserve Account are intended to cover certain shortfalls in the ability of the Issuer to service payments in relation to the Class A Debt and Class B Debt on any Interest Payment Date (excluding the repayment of principal under the Bonds and the payment of any Subordinated Coupon Amounts under the Class B Bonds). However, on any such Interest Payment Date, there are no assurances that any such shortfalls will be met in whole or in part by amounts standing to the credit of the Debt Service Reserve Account or by the DSR Liquidity Facilities.

Rights Available to Bondholders

The Bond Trust Deed contains provisions detailing the Bond Trustee's obligations to consider the interests of the Bondholders as regards all powers, trusts, authorities, duties and discretions of the Bond Trustee (except where expressly provided otherwise). Where, in the sole opinion of the Bond Trustee, there is a conflict of interest between the holders of two or more Sub-Classes of Bonds of such Class, the Bond Trustee shall consider the interests of the holders of the Sub-Class of the Class A Bonds or, if there are no Class A Bonds outstanding, the Class B Bonds outstanding with the shortest dated maturity and will not have regard to the consequences of such exercise for any other Bondholders or any other person. To the extent that the exercise of any rights, powers, trusts and discretions of the Bond Trustee affects or relates to any Class A Wrapped Bonds or Class B Wrapped Bonds, the Bond Trustee shall only act with the consent of the relevant Financial Guarantor(s) in accordance with the Bond Trust Deed. The STID provides that the Security Trustee (except in relation to certain Reserved Matters and Entrenched Rights as set out in the STID) will act on instructions of the relevant DIG Representative(s). When so doing, the Security Trustee is not required to have regard to the interests of any Finance Party (including the Bond Trustee as trustee for the Bondholders) in relation to the exercise of such rights and, consequently, has no liability to the Bondholders as a consequence of so acting.

Intercreditor Rights of Bondholders

The Bonds are subject to the provisions of the STID. The STID contains provisions enabling the Security Trustee to implement various modifications, consents and waivers in relation to the Finance Documents and the Bonds, subject to Entrenched Rights and Reserved Matters. See Chapter 7 "*Summary of the Financing Agreements*" under "*Security Trust and Intercreditor Deed – Entrenched Rights and Reserved Matters*" below. The Security Trustee is authorised to act on the instructions of the Class A DIG, or following repayment of the Class A Debt, the Class B DIG Prior to a Default Situation, a Bondholder will not be entitled to vote other than in respect of Entrenched Rights and Reserved Matters.

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

During a Default Situation the Bond Trustee shall be entitled to vote and will be entitled to seek directions from the relevant Bondholders in respect of such vote. However, the Bond Trustee may be prevented from voting if a valid Emergency Instruction Notice is delivered to the Security Trustee. See Chapter 7 "*Summary of the Financing Agreements*" under "*Emergency Instruction Procedure*". In respect of a vote relating to Entrenched Rights and Reserved Matters, the Bond Trustee will be required to seek directions from the Bondholders of each affected Series of Bonds in respect of such vote.

Accordingly, subject to the Entrenched Rights and Reserved Matters of the Bondholders, decisions relating to and binding upon the Bonds may be made by persons with no interest in the Bonds and the Bondholders may be adversely affected as a result. See Chapter 7 "*Summary of the Financing Agreements*" under "*Security Trust and Intercreditor Deed*".

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

These Entrenched Rights and Reserved Matters may materially and adversely affect the exercise and proceeds of any enforcement of the Security.

Subject to such Entrenched Rights and Reserved Matters, the Majority Creditors or, where appropriate, Super-Majority Creditors may make a modification to, or grant any consent or waiver in respect of, the Finance Documents without the need to seek a confirmation from the Rating Agencies as to the then current ratings of the Bonds.

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

There can be no assurance that a secondary market will develop, or, if a secondary market does develop for any of the Bonds issued after the date of the Prospectus, that it will provide any holder of Bonds with liquidity or that any such liquidity will continue for the life of the Bonds. Consequently, any purchaser of the Bonds must be prepared to hold such Bonds for an indefinite period of time or until final redemption or maturity of the Bonds.

The liquidity and market value at any time of the Bonds is affected by, among other things, the market view of the credit risk of such Bonds and will generally fluctuate with general interest

rate fluctuations, general economic conditions, the condition of certain financial markets, international political events, the performance and financial condition of SWS, developments and trends in the water industry generally and events in the appointed area of SWS.

Rating of the Bonds

The ratings assigned by the Rating Agencies to the Class A Wrapped Bonds and any Class B Wrapped Bonds to be issued are based solely on the claims paying ability of the applicable Financial Guarantor and reflect only the views of the Rating Agencies. The ratings assigned by the Rating Agencies to the Class A Unwrapped Bonds and the Class B Unwrapped Bonds reflect only the views of the Rating Agencies and in assigning the ratings the Rating Agencies take into consideration the credit quality of SWS and structural features and other aspects of the transaction.

A rating is not a recommendation to buy, sell or hold securities and will depend, among other things, on certain underlying characteristics of the business and financial condition of SWS or, in the case of the Wrapped Bonds, of the relevant Financial Guarantor from time to time.

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

Withholding Tax under the Bonds

In the event withholding taxes are imposed by or in any jurisdiction in respect of payments due under the Bonds, the Issuer is not obliged to gross-up or otherwise compensate Bondholders for the fact that the Bondholders will receive, as a result of the imposition of such withholding taxes, cash amounts which are less than those which would otherwise have been the case. The Issuer will, in such event, have the option (but not the obligation) of:

(i) redeeming all outstanding Bonds in full; or

(ii) arranging for the substitution of another company in an alternative jurisdiction (subject to certain conditions).

(See Chapter 8 "*The Bonds*" under "*Terms and Conditions of the Bonds*" and Condition 8(c) (*Redemption for Index Event, Taxation or Other Reasons*).)

Likewise, in the event withholding taxes are imposed in respect of payments due under the Wrapped Bonds and the relevant Financial Guarantor is called upon under its Financial Guarantee or Financial Guarantees to make payments in respect of such payments; such Financial Guarantor is not obliged to gross-up or otherwise compensate the holders of such Wrapped Bonds for the fact that such Wrapped Bondholders will receive, as a result of the

imposition of such withholding taxes, cash amounts which are less than those which would otherwise have been the case.

EU Savings Directive

The EU has adopted a Directive regarding the taxation of savings income. The Directive requires Member States to provide to the tax authorities of another Member State details of payments of interest and other similar income paid by a person to an individual in another Member State, except that Belgium, Luxembourg and Austria will instead impose a withholding system for a transitional period unless during such period they elect otherwise. A number of third countries and territories including Switzerland have adopted similar measures to the EU Directive.

Change of Law

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

European Monetary Union

Prior to the maturity of the Bonds, the United Kingdom may become a participating member state in the Economic and Monetary Union and the euro may become the lawful currency of the United Kingdom. Adoption of the euro by the United Kingdom may have the following consequences:

(i) all amounts payable in respect of the sterling denominated Bonds may become payable in euro;

(ii) the introduction of the euro as the lawful currency of the United Kingdom may result in the disappearance of published or displayed rates for deposits in sterling used to determine the rates of interest on the Bonds or changes in the way those rates are calculated, quoted and published or displayed; and

(iii) the Issuer may choose to redenominate the Bonds into euro and take additional measures in respect of the Bonds. (See Chapter 8 "*The Bonds*" under "*Terms and Conditions of the Bonds*".) The introduction of the euro could also be accompanied by a volatile interest rate. It cannot be said with certainty what effect, if any, adoption of the euro by the United Kingdom will have on investors in the Bonds.

The potential costs to SWS of implementing procedures to deal with any possible future adoption of the euro by the United Kingdom are unclear but could be significant.

Changes in Financial Reporting Standards

Certain provisions of the Transaction Documents contain certain conditions and/or triggers which are based upon an assessment of the financial condition of the SWS Financing Group calculated by reference to the financial statements produced in respect of the companies in the SWS Financing Group. These financial and other covenants have been set at levels which are based on the current accounting principles, standards, conventions and practices adopted by the relevant companies.

It is possible that any future changes in these accounting principles, standards, conventions and practices which are adopted by the companies in the SWS Financing Group may result in significant changes in the reporting of its financial performance (e.g. "FRS26: Financial Instruments: Measurement" and the introduction of International Financial Reporting). This, in turn, may necessitate that the terms of the conditions and triggers referred to above are renegotiated.

Funding Risks in relation to the Defined Benefits under the Pension Schemes

The two pension schemes which operate predominantly for SWS employees are the SWPS and a CSP. The SWPS is a funded defined benefit arrangement and the CSP is a defined contribution scheme.

The primary liability for funding the SWPS and the CSP (together, the "**Pension Schemes**") rests with SWS. By virtue of the Pensions Act 2004, there will be risks for SWS Financing Group arising from the operation of the Pension Schemes. Many of these are generic risks associated with the operation of UK defined pension schemes generally.

In summary, the main risk factors are:

(a) The Pensions Act 2004 will allow the Pensions Regulator to impose a scheme funding target and employer contribution rate if those matters cannot be agreed between the scheme trustees and the employers and is expected to result in more onerous funding requirements for employers.

(b) The trustees of each Pension Scheme have power to wind up the relevant scheme in certain circumstances (e.g. if they think it unlikely that sufficient funding will be available to provide all benefits in full). As a result of recent changes in legislation, winding up the schemes would result in a statutory obligation on the various participating employers to fund the schemes by reference to a "buy-out basis". Additionally, regulations provide that a similar statutory debt would be triggered if SWS went into liquidation.

(c) The Pensions Act 2004 gives new powers to the Pensions Regulator to require funding or funding guarantees for defined benefit pension schemes from any company in the same group as the participating employers. This applies regardless of whether the companies sought to be made liable have any employees in the pension schemes concerned.

(d) The trustees of each Pension Scheme have control over the investment of the relevant scheme's assets and could (having taken appropriate investment advice and consulted with the employers) alter the investment profile of the schemes. For example, they could exchange equity investments for bonds, which would typically increase the employer funding obligations in relation to the schemes because of the lower rate of return expected from lower risk bonds.

The foregoing risks are linked to the funding level of the schemes, which can be adversely affected by a number of factors including:

(i) reducing bond yields (low yields mean a pension obligation is assessed as having a high value);

(ii) increasing life expectancy (which will make pensions payable for longer and, therefore, more expensive to provide);

(iii) investment returns below expectation;

(iv) actual and expected price inflation (many benefits are linked to price inflation and, ignoring any compensating change in the value of assets and future expected investment returns, an increase in inflation will result in higher benefits being paid);

(v) funding volatility as a result of the mismatch between the assets held and the assets by reference to which the scheme liabilities are calculated; and

(vi) other events occurring which make past service benefits more expensive than anticipated in the actuarial assumptions by reference to which past pension contributions were assessed, including unanticipated changes to legislation or tax laws.

Employer obligations to their pension schemes (including any statutory debt) generally rank as unsecured and non-preferential obligations of the employer, with some limited exceptions.

Trading in the Clearing systems - integral multiples of less than €50,000

Although Bonds which are admitted to trading on a regulated market in the European Economic Area or offered to the public in a Member State of the European Economic Area in circumstances which require the publication of a prospectus under the Prospectus Directive are required to have a minimum denomination of €50,000 (or, where the specified currency is not euro, its equivalent in the specified currency), it is possible that the Bonds may be traded in the clearing systems in amounts in excess of €50,000 (or its equivalent) that are not integral multiples of €50,000 (or its equivalent). In such a case, should definitive Bonds be required to be issued, a holder who does not have an integral multiple of €50,000 (or its equivalent) in his account with the relevant clearing system at the relevant time may not receive all of his entitlement in the form of definitive Bonds unless and until such time as his holding becomes an integral multiple of €50,000 (or its equivalent).

CHAPTER 6
WATER REGULATION

Water Regulation Generally

Regulatory Framework

The activities of a company which is appointed as a water undertaker or a water and sewerage undertaker under section 6 of the WIA (a "Regulated Company") are principally regulated by the provisions of the WIA (as amended by subsequent regulation, including the Water Act 2003), regulations made under the WIA and the conditions of their appointments as water undertakers and sewerage undertakers (together "licences" and each a "licence"). Under the WIA, the Secretary of State has a duty to ensure that at all times there is a Regulated Company for every area of England and Wales. Appointments may be made by the Secretary of State or, in accordance with a general authorisation given by him/her, the WSRA (as defined below).

The economic regulator for water is the WSRA (which replaced the role of the DGWS from 1 April 2006) which is aided in its duties by Ofwat, a non-ministerial government department, of which it is head. The WSRA is responsible for, among other things, setting limits on charges and monitoring and enforcing licence obligations. Regulated Companies are required by their licences to make an annual return to Ofwat (including accounts and financial information) to enable Ofwat to assess their affairs. The two principal quality regulators are the Drinking Water Inspectorate (the "DWI"), which is part of DEFRA, and the EA.

The WSRA and the Secretary of State

The WSRA is appointed for a fixed term by the Secretary of State. It is independent of government ministers and may only be removed for incapacity or misbehaviour.

Each of the Secretary of State and the WSRA has a primary duty under the WIA to exercise and perform its powers and duties under the WIA in the manner it considers best calculated to secure that, inter alia:

- the functions of Regulated Companies are properly carried out throughout England and Wales;
- Regulated Companies are able (in particular, by securing reasonable returns on their capital) to finance the proper carrying out of those functions; and
- the "consumer objective", defined as the protection of consumers' interests (where appropriate by promoting competition), with particular emphasis upon certain categories of customers, is furthered.

Subject to this primary duty, each of the Secretary of State and the WSRA is required to exercise and perform its powers and duties in the manner it considers best calculated to:

- protect the interests of customers (especially rural customers) in connection with the fixing and recovery of water and drainage charges, such that no undue preference or discrimination is shown in the fixing of those charges;

- protect the interests of customers in connection with the terms on which services are provided and the quality of those services;

- protect the interests of customers as regards non-regulated activities of Regulated Companies (and companies connected with them) in particular by ensuring that (i) transactions are carried out at arm's length; and (ii) in relation to their Appointed Business, Regulated Companies maintain and present accounts in a suitable form and manner;

- protect the interests of customers in connection with the benefits that could be secured for them by the disposal by Regulated Companies of "Protected Land";

- promote economy and efficiency on the part of Regulated Companies;

- facilitate effective competition between Regulated Companies and those seeking appointments as Regulated Companies; and

- promote economy and efficiency on the part of the Regulated Companies and contribute to the achievement of sustainable development.

In addition, there is provision for guidance to be issued by the Secretary of State to the WSRA on social and environmental matters. Once guidance has been issued in accordance with the prescribed process, the WSRA would be obliged to have regard to that guidance in carrying out its functions.

Customers' Interests

The WSRA regulates prices (see "Economic Regulation" below) and also monitors certain aspects of service performance. Regulated Companies are also subject to a statutory "Guaranteed Standards Scheme" which provides for compensation to be paid to customers in the event that certain minimum service requirements are not met.

Until 1 October 2005, customers' interests were also served by regional Ofwat Customer Service Committees (usually known as "WaterVoice") which reviewed all matters relating to the interests of customers and investigated complaints made by customers against companies. The WaterVoice Council, comprised of Chairmen from the regional committees, represented all water customers at the national and European levels, and advised the DGWS on the development of policy.

On 1 October 2005 the functions of the WaterVoice committees were transferred to a new independent Consumer Council for Water ("CCW"), created in accordance with the provisions of the WIA as amended by the Water Act 2003, and headed by a Chairman appointed by the

Secretary of State. The CCW has been granted various additional powers and functions, including the right to be provided with certain information by Regulated Companies.

Licences

Under the WIA, each Regulated Company holds a licence and is regulated through the conditions of such licence as well as the WIA. Each licence specifies the geographic area served by the company and imposes a number of conditions on the licence holder which relate to the determination and regulation of price limits and other matters (see below). The main provisions of SWS's Licence are typical of those of all licences of Regulated Companies. The WSRA is responsible for monitoring compliance with the conditions of the licence and, where necessary, enforcing compliance through procedures laid down in the WIA (see "Enforcement Orders" below).

In addition to the conditions regulating price limits (see "Economic Regulation" below), the Licence also contains conditions regulating infrastructure charges and the making of charges schemes, and imposes prohibitions on undue discrimination and undue preference in charging. Other matters covered by the Licence include (but are not limited to) provisions in relation to: accounts and the provision of accounting information (including a requirement to prepare and publish accounts showing the Appointed Business separately from all other businesses and activities); provisions governing the "financial ring-fencing" of SWS, transactions with associated companies (as defined by the Licence), certain restrictions as to the indebtedness entered into or provided by SWS, certain conditions as to the payment of dividends; a requirement that SWS has at its disposal sufficient financial and managerial resources to carry out its regulated activities; a requirement that SWS must at all times conduct its Appointed Business as if such business were substantially its sole business and SWS were a separate public limited company, including requirements as to corporate governance arrangements and maintenance of a listed financial instrument; and a requirement that SWS, or any associated company (as defined by the Licence) issuing corporate debt on its behalf, uses all reasonable endeavours to ensure that it maintains an investment grade issuer credit rating in relation to corporate debt. Further matters covered by the Licence include: provisions relating to levels of service and service targets; restrictions on disposal of land; asset management plans; the payment of fees to Ofwat and payments to customers for supply interruptions because of drought; an obligation to prepare drought plans, to agree them with the Secretary of State and to make them publicly available; and an obligation to agree water resource management plans with the Secretary of State and to make them publicly available.

Termination of a licence

There are certain circumstances provided for in the WIA under which a Regulated Company could cease to hold a licence for all or part of its area:

- a Regulated Company could consent to the making of a replacement appointment or variation, which changes its appointed area, in which case the WSRA has the authority to appoint a new licence holder;

- under condition O of the licence, provided at least 25 years' notice has been given by the Secretary of State;
- under the provisions of the special administration regime (the licence may be terminated and the Special Administrator may transfer the business to a successor (see "Special Administration Orders" below)); or
- by the granting of an "inset" appointment over part of a Regulated Company's existing appointed area to another Regulated Company (see below).

Before making an appointment or variation replacing a Regulated Company, the WSRA or the Secretary of State must consider any representations or objections made. In making an appointment or variation replacing a Regulated Company and where the Secretary of State or WSRA is to determine what provision should be made for fixing charges, it is the duty of the Secretary of State or the WSRA to ensure, so far as may be consistent with their duties under the WIA, that the interests of the members and creditors of the existing Regulated Company are not unfairly prejudiced as regards the terms on which the new Regulated Company could accept transfers of property, rights and liabilities from the existing Regulated Company.

An "inset" appointment can be granted to a company seeking to provide water and/ or sewerage services on a greenfield site, or to a large user of water and/or sewerage services within an existing Regulated Company's area, or where the incumbent Regulated Company consents to the variation. The threshold for large user insets in England is 50 megalitres of water per annum.

Modification of a licence

There are a number of circumstances in which the conditions of a licence can be modified. These include any specific powers to make certain modifications which are granted by Parliament to give effect to new legislation. In addition, the Water Act 2003 provides for licences to be modified to provide a new duty to further water conservation.

Enforcement Orders

The general duties of Regulated Companies are enforceable by the Secretary of State or the WSRA or both. The conditions of each licence (and other duties) are enforceable by the WSRA alone whilst other duties, including those relating to water quality, are enforceable by the Secretary of State.

Where the Secretary of State or the WSRA is satisfied that a Regulated Company is contravening, or has contravened and is likely to do so again, its licence, or a relevant statutory or other requirement, either the Secretary of State or the WSRA must make a final enforcement order to secure compliance with that condition or requirement, save that, where it appears to the Secretary of State or the WSRA more appropriate to make a provisional enforcement order, he may do so. In determining whether a provisional enforcement order should be made, the Secretary of State or WSRA shall have regard to the extent to which any person is likely to sustain loss or damage as a consequence of such breach before a final enforcement order is made. The Secretary of State or the WSRA will confirm a provisional enforcement order if

satisfied that the provision made by the order is needed to ensure compliance with the condition or requirement which is in breach.

There are exemptions from the Secretary of State's and the WSRA's duty to make an enforcement order or to confirm a provisional enforcement order:

- where the contraventions were, or the apprehended contraventions are, of a trivial nature;
- where the company has given, and is complying with, an undertaking to secure or facilitate compliance with the condition or requirement in question; or
- where duties in the WIA preclude the making or confirmation of the order.

Financial Penalties

The WIA provides the WSRA, the Secretary of State and the National Assembly for Wales with the power to impose financial penalties on a Regulated Company for contraventions of its Conditions of Appointment and statutory or other requirements including performance standards. Penalties may be as high as 10 per cent. of a Regulated Company's turnover, but they must be reasonable in all circumstances. Each of the above enforcement authorities is required to publish a statement of policy on the imposition of penalties, and to have regard to that statement when implementing the new provisions. Such a statement of policy with respect to financial penalties was published jointly by Ofwat, DEFRA and the National Assembly for Wales in March 2005.

Special Administration Orders

The WIA contains provisions enabling the Secretary of State or the WSRA, with the consent of the Secretary of State, to secure the general continuity of water supply and sewerage services. In certain specified circumstances, the High Court (the "Court") may, on the application of the Secretary of State or, with his consent, the WSRA, make a Special Administration Order in relation to a Regulated Company and appoint a Special Administrator. These circumstances include:

- where there has been, or is likely to be, a breach by a Regulated Company of its principal duties to supply water or provide sewerage services or of a final or confirmed provisional enforcement order and, in either case, the breach is serious enough to make it inappropriate for the Regulated Company to continue to hold its licence;
- where the Regulated Company is, or is likely to be, unable to pay its debts;
- where, in a case in which the Secretary of State has certified that it would be appropriate, but for Section 25 of the WIA, for him to petition for the winding up of the Regulated Company under section 440 of the Companies Act 1985, it would be just and equitable, as mentioned in that section, for the Regulated Company to be wound up if it did not hold a licence; and
- where the Regulated Company is unable or unwilling adequately to participate in arrangements certified by the Secretary of State or the WSRA to be necessary by reason

of, or in connection with, the appointment of a new Regulated Company upon termination of the existing Regulated Company's licence.

In addition, on an application being made to a court, whether by the Regulated Company itself or by its directors, creditors or contributories, for the compulsory winding up of the Regulated Company, a court would not be entitled to make a winding up order; however, if satisfied that it would be appropriate to make such an order if the Regulated Company were not a company holding a licence, a court shall instead make a Special Administration Order.

During the period beginning with the presentation of the petition for Special Administration and ending with the making of a Special Administration Order or the dismissal of the petition (the "Special Administration Petition Period"), the Regulated Company may not be wound up, no steps may be taken to enforce any security except with the leave of the Court, and subject to such terms as the Court may impose, and no other proceedings or other legal process may be commenced or continued against the Regulated Company or its property except with the leave of the Court.

Once a Special Administration Order has been made, any petition presented for the winding up of the company will be dismissed and any receiver appointed, removed. Whilst a Special Administration Order is in force, those restrictions imposed during the Special Administration Petition Period continue with some modifications: an administrative receiver can no longer be appointed (with or without the leave of the Court) and, where any action does require the Court's leave, the consent of the Special Administrator is acceptable in its place (see "Restrictions on the enforcement of security" below).

A Special Administrator has extensive powers under the WIA similar to those of an administrator under English insolvency law applicable to companies which are not Regulated Companies, but with certain important differences. A Special Administrator would be charged with managing the affairs, business and property of the Regulated Company: (i) for the achievement of the purposes of the Special Administration Order; and (ii) in such a manner as protects the respective interests of the members and creditors of the Regulated Company. The purposes of the Special Administration Order consist of: (a) transferring to one or more different Regulated Companies, as a going concern, as much of the business of the Regulated Company as is necessary in order to ensure that the functions which have been vested in the Regulated Company by virtue of its licence are properly carried out; and (b) pending the transfer, the carrying out of those functions. It would therefore not be open to him to accept an offer to purchase the assets on a break-up basis in circumstances where the purchaser would be unable properly to carry out the relevant functions of a Regulated Company.

The powers of a Special Administrator include, as part of a Transfer Scheme, the ability to make modifications to the licence of the existing Regulated Company, subject to the approval of the Secretary of State or the WSRA. The Special Administrator agrees the terms of the transfer of the existing Regulated Company's business to the new Regulated Company (ies), on behalf of the existing Regulated Company. The transfer is effected by a Transfer Scheme which the Special Administrator puts in place on behalf of the existing Regulated Company. The Transfer Scheme may provide for the transfer of the property, rights and liabilities of the existing Regulated Company to the new Regulated Company(ies) and may also provide for the transfer of

the existing Regulated Company's licence (with modifications as set out in the Transfer Scheme) to the new Regulated Company(ies). The powers of a Special Administrator include the right to seek a review by the WSRA of the Regulated Company's charges pursuant to an IDOK or a "Shipwreck Clause" (as defined below). To take effect, the Transfer Scheme must be approved by the Secretary of State or the WSRA. In addition, the Secretary of State and the WSRA may modify a Transfer Scheme before approving it or at any time afterwards with the consent of the Special Administrator and each new Regulated Company.

The WIA also grants the Secretary of State, with the approval of the Treasury, the power: (i) to make appropriate grants or loans to achieve the purposes of the Special Administration Order or to indemnify the Special Administrator against losses or damages sustained in connection with the carrying out of his functions; and (ii) to guarantee the payment of principal or interest or the discharge of any other financial obligations in connection with any borrowings of the Regulated Company subject to a Special Administration Order.

Protected Land

Under the WIA, there is a prohibition on Regulated Companies disposing of any of their Protected Land except with the specific consent of, or in accordance with a general authorisation given by, the Secretary of State. A consent or authorisation may be given on such conditions as the Secretary of State considers appropriate. For the purpose of these provisions, disposal includes the creation of any interest (including leases, licences, mortgages, easements and wayleaves) in or any right over land, and includes the creation of a charge. All land disposals are reported to Ofwat in the annual return.

Protected Land comprises any land, or any interest or right in or over any land, which:

- was transferred to a water and sewerage company (under the provisions of the Water Act 1989) on 1 September 1989, or was held by a water only company at any time during the financial year 1989-90;
- is, or has at any time on or after 1 September 1989 been held by a company for purposes connected with the carrying out of its regulated water or sewerage functions; or
- has been transferred to a company in accordance with a scheme under Schedule 2 to the WIA from another company, in relation to which the land was Protected Land when the transferring company held an appointment as a water or sewerage undertaker.

Security

Restrictions on the granting of security

A Regulated Company's ability to grant security over its assets and the enforcement of such security are restricted by the provisions of the WIA and its licence. For example, all licences (including the Licence) restrict a Regulated Company's ability to dispose of Protected Land (as explained in "Protected Land" above). Accordingly, a licence restricts a Regulated Company's ability to create a charge or mortgage over Protected Land. In the case of SWS, management believes that the vast majority of SWS' assets by value is tangible property which is Protected

Land and cannot therefore be effectively secured. This necessarily affects the ability of SWS to create a floating charge over the whole or substantially the whole of its business. Furthermore, in any event, there is no right under the WIA to block the appointment of a Special Administrator equivalent to the right which a holder of a floating charge over the whole or substantially the whole of the business of a company which is not a Regulated Company may have in certain circumstances to block the appointment of a conventional administrator.

In addition, provisions in a Regulated Company's licence require the Regulated Company at all times:

- to ensure, so far as is reasonably practicable, that if a Special Administration Order were made in respect of it, it would have sufficient rights and assets (other than financial resources) to enable the Special Administrator to manage its affairs, business and property so that the purpose of such order could be achieved; and

- to act in the manner best calculated to ensure that it has adequate: (i) financial resources and facilities; and (ii) management resources, to enable it to carry out its regulated activities.

These provisions may further limit the ability of SWS to grant security over its assets and may limit in practice the ability to enforce such security.

Restrictions on the enforcement of security

Under the WIA, the enforcement of security given by a Regulated Company in respect of its assets is prohibited unless the person enforcing the security has first given 14 days' notice to both the Secretary of State and the WSRA. If a petition for Special Administration has been presented, leave of the Court is required before such security is enforceable or any administrative receiver can be appointed (or, if an administrative receiver has been appointed between the expiry of the required notice period and presentation of the petition, before the administrative receiver can continue to carry out his functions). These restrictions continue once a Special Administration Order is in force with some modification (see "Special Administration Orders" above).

Once a Special Administrator has been appointed, he would have the power, without requiring the Court's consent, to deal with property charged pursuant to a floating charge as if it were not so charged. When such property is disposed of under this power, the proceeds of the disposal would, however, be treated as if subject to a floating charge which had the same priority as that afforded by the original floating charge.

A disposal by the Special Administrator of any property secured by a fixed charge given by the Regulated Company could be made only under an order of the Court unless the creditor in respect of whom such security is granted otherwise agreed to such disposal. Such an order could be made if, following an application by the Special Administrator, the Court was satisfied that the disposal would be likely to promote one or more of the purposes for which the order was made (although the Special Administrator is subject to the general duty to manage the company in a manner which protects the respective interests of the creditors and members of the Regulated

Company). Upon such disposal, the proceeds to which that creditor would be entitled would be determined by reference to the "best price which is reasonably available on a sale which is consistent with the purposes of the Special Administration Order" as opposed to an amount not less than "open market value" which would apply in a conventional administration for a non-Regulated Company under English insolvency legislation.

Within three months of the making of a Special Administration Order or such longer period as the Court may allow, the Special Administrator must send a copy of his proposals for achieving the purposes of the order to, among other things, the Secretary of State, the WSRA and the creditors of the company. The creditors' approval to the Special Administrator's proposal is not required at any specially convened meeting (unlike in the conduct of a conventional administration for a non-Regulated Company under English insolvency legislation); however, notwithstanding this, the interests of creditors and members in a Special Administration are still capable of being protected since they have the right to apply to the Court if they consider that their interests are being prejudiced. Such an application may be made by the creditors or members by petition for an order on a number of grounds, including either: (i) that the Regulated Company's affairs, business and property are being or have been managed by the Special Administrator in a manner which is unfairly prejudicial to the interests of its creditors or members; or (ii) that any actual or proposed act of the Special Administrator is/or would be so prejudicial. Any order made by the Court may include an order to require the Special Administrator to refrain from doing or continuing an act about which there has been a complaint.

Enforcement of Security over Shares in SWS

Under the WIA, the enforcement of security over, and the subsequent sale of, directly or indirectly, the shares in any group company, including those of a Regulated Company such as SWS, would not be subject to the restrictions described above in relation to the security over SWS' business and assets. Notwithstanding this, given the WSRA's general duties under the WIA to exercise and perform its powers and duties, among other things, to ensure that the functions of a Regulated Company are properly carried out, management anticipates that any intended enforcement either directly or indirectly of the security granted by SWSGH and/or SWSH or the security over, and subsequently any planned disposal of, the shares in SWS to a third party purchaser, would require consultation with the WSRA. In addition, depending on the circumstances, the merger control provisions referred to in "Competition in the Water Industry - Merger Regime" (below) could apply in respect of any such disposal. However, no such consultation process would be required for the enforcement of the security over preference shares in relation to the Facility.

Economic Regulation

Economic regulation of the water industry in England and Wales is based on a system of five-year price caps imposed on the amounts Regulated Companies can charge to their customers. This is intended to reward companies for efficiency and quality of service to customers. The system generally allows companies to retain for a period any savings attributable to efficiency, thus creating incentives to make such gains.

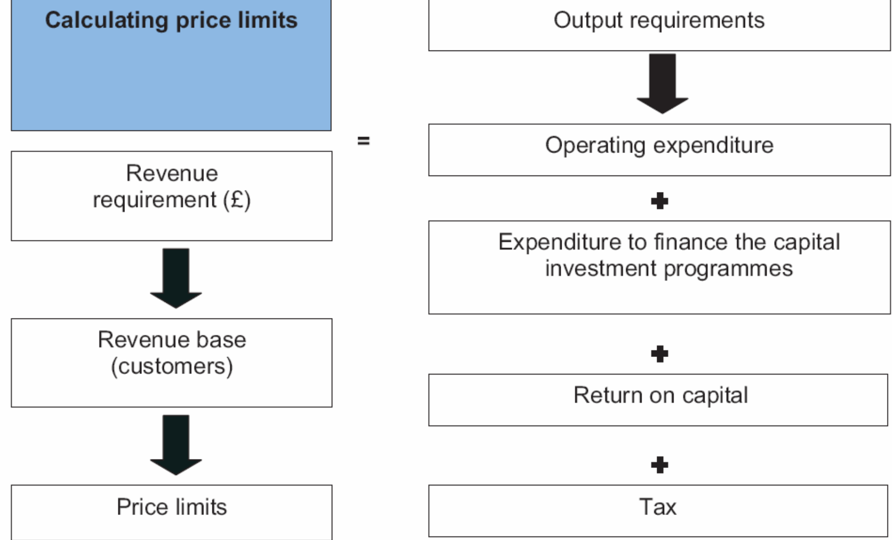
As shown diagrammatically below, Ofwat uses a building block approach to calculate revenue companies can earn (and therefore the prices customers are charged). The four building blocks are:

- Return on RCV (26% SWS's 2005/6 turnover). Ofwat calculates cost of capital using a notional balance sheet geared at 55% (i.e. companies' specific capital structures are not taken into account). Water only companies are allowed an additional 0.5% 'small company premium';

- Operating costs (35%) are calculated with reference to prior years. Ofwat then applies an efficiency target based on comparative data;

- Current cost depreciation (37%); and

- Taxation (2%). Companies are funded at their actual tax rate (being the only part of the price setting process that reflects actual capital structures).



Ofwat uses comparative data to establish efficiency targets for both operating expenditure and capital expenditure – efficient companies are given softer targets. Ofwat's ability to compare company performance is an integral part of the price setting process.

The following table sets out Ofwat's determinations of price limits for the period 2005 to 2010. Ofwat considers that these price limits should enable companies to deliver their outputs, but are no higher than they need to be in the interests of customers.

			Annual price limits			
Company	**2005-06**	**2006-07**	**2007-08**	**2008-09**	**2009-10**	**Average[1]**
Water and Sewerage companies (WaSC)						
Anglian	3.8	0.0	2.8	2.7	2.7	2.4
Dŵr Cymru	14.2	3.6	4.1	3.3	2.2	5.4
Northumbrian	6.5	3.7	3.2	1.0	0.6	3.0
Severn Trent	11.8	4.8	2.0	1.7	2.3	4.5
South West	12.5	9.8	9.8	1.7	1.4	6.9
Southern	12.6	3.9	3.5	5.8	2.6	5.6
Thames	14.9	2.1	1.2	1.3	1.5	4.1
United Utilities	5.0	6.4	4.4	3.5	3.0	4.5
Wessex	8.9	4.9	5.6	4.0	2.9	5.2
Yorkshire	5.5	4.9	3.6	3.6	2.1	3.9
WaSC average (Weighted)	9.4	4.0	3.4	2.7	2.2	4.3

Source: Final determinations for future water and sewerage charges 2005-2010 published by Ofwat

Note 1: the average for the price limits is the geometric average of the annual price limits

K price limitation formula

The main instrument of economic regulation is the framework of price limits set out in the conditions of the licences. These act to limit increases in a basket of standard charges made by Regulated Companies for water supply and sewerage services. The weighted average charges increase is limited to the sum of the percentage movement in the RPI plus K. K (a factor which can be a positive, negative or zero) is a number set by the WSRA for each Regulated Company individually and may be a different number in different years. Certain charges are not included in the price limitation formula but are determined on an individual basis.

Regulatory Capital Value

Under the methodology developed by Ofwat, the regulatory capital value of Regulated Companies is a critical parameter underlying price limits set at Periodic Reviews, being the value of the capital base of the relevant Regulated Company for the purposes of calculating the return on capital element of the determination of K. The value of the regulatory capital value to investors and lenders is protected against inflation by increasing the value each year by RPI.

In addition, Ofwat's projections of regulatory capital value take account of the assumed net capital expenditure in each year of a Periodic Review Period. For these purposes, Ofwat make an assumption regarding the relationship between movements in RPI and movements in the Construction Output Prices Index ("COPI"). At the 2004 Periodic Review, Ofwat adjusted SWS'

RCV for the difference between their previous assumptions regarding this relationship and the actual relationship to 2004. Ofwat also made assumptions about the relative movement of the two indices between 2005 and 2009. At the 2009 Periodic Review SWS' RCV will again be adjusted by, amongst other things, substituting the actual movement in COPI for that assumed in 2004. References in this Prospectus to 'out-turn' prices are to 2002/03 prices using the same assumptions regarding the relationship between RPI and COPI as those used by Ofwat for the 2004 Periodic Review.

Price Control

A small number of mainly large consumption non-domestic customers are charged in accordance either with individual "special" arrangements, or with standard charges which do not fall within the scope of the tariff basket. These include charges for bulk supplies and infrastructure charges and, where these are not in accordance with standard charges, charges for non-domestic supplies of water and the reception, treatment and disposal of trade effluent. Charges for bulk supplies of water are usually determined on an individual basis, as are charges for some larger non-domestic water supplies and some trade effluent. The charging basis for bulk supplies in some cases provides for annual recalculation by reference to the expenditure associated with the supply.

Periodic Reviews of K

K is reviewed every five years. Following the last Periodic Review, new price limits took effect from 1 April 2005 and are set for the five year period from 2005 to 2010. The WSRA will next reset price limits in 2009 and these will come into effect on 1 April 2010.

Interim Determinations of K

Condition B of a Regulated Company's licence provides for the WSRA to determine in certain circumstances whether, and if so how, K should be changed between periodic reviews. The procedure for an IDOK can be initiated either by the Regulated Company or by the WSRA. An application for an IDOK may be made in respect of a Notified Item (see below), a Relevant Change of Circumstance (see below), or a substantial adverse or favourable effect on the Appointed Business (see below).

A "Notified Item" is any item formally notified by the WSRA to the Regulated Company as not having been allowed for in full or in part in K at the last price determination. Notified Items put forward by the WSRA in the determination of price limits for the period 2005 to 2010 were: (i) the costs and revenues associated with any difference in the number of Meter Optants from that assumed by the WSRA; (ii) any net increase in bad debt and debt collection costs arising from the loss of the power to disconnect residential customers for non-payment from 1 April 2000; (iii) increases in charges for abstractions and for discharges to controlled waters; (iv) charges for lane rental/traffic management; and (v) increases in the taxation of infrastructure expenditure arising from the introduction of International Financial Reporting Standards (IFRS).

"Relevant Changes of Circumstance" are defined in the licences. Such changes include: (i) the application to the Regulated Company of any new or changed legal requirement (including any legal requirement ceasing to apply, being withdrawn or not being renewed); (ii) any difference in value between actual or anticipated proceeds of disposals of land and those allowed for at the last

Periodic Review or IDOK; and (iii) the amounts assumed in K for the necessary costs of securing or facilitating compliance with a legal requirement or achieving a service standard where the Regulated Company has failed to: (a) carry out the necessary works; (b) spend the amount which it was assumed would be spent; and (c) achieve the stated purpose.

An IDOK takes account of the costs, receipts and savings to be included in the computation of K which are reasonably attributable to the Notified Items or the Relevant Changes of Circumstance in question and are not recoverable by charges outside the K price limitation formula. The amount and timing of the costs, receipts and savings must be appropriate and reasonable for the Regulated Company in all the circumstances and they must exclude: trivial amounts, any costs which would have been avoided by prudent management action, any savings achieved by management action over and above those which would have been achieved by prudent management action, and any amounts previously allowed for in determining K. These costs are then netted off against the receipts and savings to determine the Base Cash Flows for each year included in the timing.

The conditions of the licences also specify a materiality threshold which must be reached before any adjustment can be made. In relation to certain licences (including that of SWS), this materiality threshold is currently reached where the sum of the net present values of (i) Base Cash Flows consisting of operating expenditure and/or loss of revenue calculated over 15 years and (ii) other Base Cash Flows calculated over the period to the next periodic review, is equal to at least 10 per cent. of the latest reported turnover attributable to the Regulated Company's water and sewerage business (though, in "Future water and sewerage charges 2005-2010 Final Determinations" Ofwat states that it will consider how best to modify the existing materiality calculation and will consult further on this). An adjustment to K (which may be up or down) is then calculated on the basis of a formula broadly designed to enable the Regulated Company to recover the Base Cash Flows. The change is then made for the remainder of the period up to the start of the first charging year of the next five-year price control period. Condition B of each licence sets out in detail the step-by-step methodology which the WSRA is required to apply.

Substantial Adverse or Favourable Effects – Shipwreck Clause

SWS, similarly to certain other Regulated Companies, may, under specific conditions of the Licence (the "Shipwreck Clause"), request price limits to be reset if the Appointed Business suffers a substantial adverse effect which could not have been avoided by prudent management action. The WSRA may, similarly, reset price limits if the Appointed Business enjoys a substantial favourable effect which is fortuitous and not attributable to prudent management action. For the purpose of the Shipwreck Clause the materiality threshold is equal to at least 20 per cent. (as opposed to 10 per cent. for a determination made in respect of Notified Items and Relevant Changes of Circumstances) of the latest reported turnover attributable to the Regulated Company's water and sewerage business.

References to the Competition Commission

If the WSRA fails within specified periods to make a determination at a Periodic Review or in respect of an IDOK or if the Regulated Company disputes its determination, the Regulated Company may require the WSRA to refer the matter to the Competition Commission (the "CC").

The CC must make its determination in accordance with any regulations made by the Secretary of State and with the principles which apply, by virtue of the WIA, in relation to determinations made by the WSRA. The decisions of the CC are binding on the WSRA.

Drinking Water and Environmental Regulation

The water industry is subject to numerous regulatory requirements concerning the protection of the environment and human health and safety. Responsibility for regulation of drinking water quality and environmental standards lies with the DWI and the EA respectively.

The DWI is part of the DEFRA and acts as a technical assessor on behalf of the Secretary of State in respect of the quality of drinking water supplies. It can take enforcement action in the event that a water undertaker is in contravention of regulatory requirements concerning the "wholesomeness" of water supplies. Court proceedings can be brought for the offence of supplying water "unfit for human consumption", for example if discoloured or foul tasting water is supplied to customers.

The EA is responsible in England and Wales for the licensing of water abstraction, the control of water pollution and the maintenance and improvement of the quality of controlled waters, including the regulation of discharges to those waters. The principal UK environmental legislation relevant to Regulated Companies includes the Water Resources Act 1991 (the "WRA"), the Environmental Protection Act 1990 (the "EPA") and the WIA. The Water Act 2003 amends both the WRA and the WIA (see "The Water Act 2003" below).

Under the WRA any discharge of trade or sewage effluent into controlled waters can only be carried out with a discharge consent from the EA or with some other lawful authority. The discharge consent system under the WRA is backed up by various criminal offences. It is a criminal offence to cause or knowingly permit polluting matter to enter controlled waters. The principal prosecuting body is the EA. Under the WRA, the EA is empowered to take remedial action to deal with actual or potential pollution of controlled waters and may recover the reasonable costs of such works from the person who caused or knowingly permitted the pollution (and can also require that person to take the remedial action itself).

Sewerage undertakers are responsible under the WIA for regulating discharges of industrial effluent into sewers. In addition, discharges from sewage treatment works must be licensed by the EA. Contamination of controlled waters by discharge of non-compliant effluent from a treatment works may expose the sewerage undertaker to liability, including fines and clean-up costs. The EA publicises breaches by Regulated Companies of their discharge consents and brings prosecutions where necessary.

The EPA (supported by implementing regulations and statutory guidance), introduced a regime to deal with the remediation of contaminated land. Under the regime, the causer or knowing permitter of the pollution (or, if that person cannot be found, the owner or occupier of the land) can be required to clean up contamination if it is causing, or there is a significant possibility of it causing, significant harm to the environment or human health or if pollution of controlled waters is being caused. Civil liability may also arise (under such heads of claim as nuisance and

negligence) where contamination migrates into the environment at third party land and/or impacts upon human health, flora and fauna.

Any expenditure incurred by a Regulated Company necessitated by legislation applying to it in its capacity as a water or sewerage undertaker, or by any change in consents as a result of any changes to existing EU directives, or adoption of future EU directives, would be eligible for consideration for an IDOK, or to be taken into account at a periodic review.

The Water Act 2003

The Water Act 2003 (the "Water Act") received Royal Assent on 20 November 2003 and has substantially come into force.

Modifications to the General Duties of the Secretary of State and the WSRA

The Water Act puts forward a number of amendments to the statutory duties of the Secretary of State and the WSRA referred to above (see "The WSRA and the Secretary of State").

It adds to the primary duties referred to above a duty to "further the consumer objective". This, in turn, is defined as the protection of the interests of consumers, wherever appropriate, by promoting effective competition. Particular regard is to be had to the interests of specific groups of customers, such as pensioners and those residing in rural areas. The list of additional duties is amended, among other things, to require the Secretary of State and the WSRA to exercise their powers to "contribute to the achievement of sustainable development".

There is provision for guidance to be issued by the Secretary of State to the WSRA on social and environmental matters. Once guidance has been issued in accordance with the prescribed process, the WSRA is obliged to have regard to that guidance in carrying out its functions.

New Regulatory Arrangements

The Water Act provides for a number of changes to existing regulatory arrangements:

- the WSRA has been replaced by the Water Services Regulation Authority (the "WSRA"). The WSRA consists of a chairman and at least two other members appointed by the Secretary of State;

- the existing Customer Service Committees, which had been established under the WIA by the DGWS, have been abolished, and replaced by a new independent "Consumer Council for Water" ("CCW"), under a chairman appointed by the Secretary of State. Regional committees of the CCW cover one or more Regulated Companies. The CCW has a range of functions and duties relating to the promotion of customers' interests. It also has powers to obtain information from Regulated Companies;

- the WSRA and the Secretary of State have been given a new power to impose financial penalties on a Regulated Company for contraventions of its licence, statutory or other requirements, including performance standards. A penalty must be reasonable in all the circumstances and be no more than 10 per cent. of a Regulated Company's turnover. The

WSRA and Secretary of State have the power to make an enforcement order where a contravention is likely (whether or not one has previously occurred) as well as where one is occurring. The WSRA and Secretary of State are each required to publish and have regard to a statement of policy on the implementation of penalties. Such a statement of policy with respect to financial penalties was published jointly by Ofwat, DEFRA and the National Assembly for Wales in March 2005; and

- there is a new obligation on Regulated Companies to disclose arrangements linking the remuneration of directors of the company to the achievement of performance standards.

Modification of a licence without consent

The Water Act sets out two special circumstances where the conditions of appointment may be modified without the consent of the Regulated Company:

- Ofwat has the power to modify conditions of appointment to provide for the recovery of the expenses of the new CCW. Ofwat will be required to consult Regulated Companies before making such modifications, and can only exercise the power within two years of commencement of these provisions on 1 April 2004. The exercise of the power is also subject to directions by the Secretary of State; and

- Ofwat will have the power to modify conditions of appointment to give effect to the new provisions for competition (see below “New Framework for Competition”). Ofwat has to consult Regulated Companies and other persons who may be affected, and the exercise of their power is again subject to a two year time limit and any directions made by the Secretary of State.

Other Provisions

The Water Act contains numerous additional provisions which will or may affect Regulated Companies. These include, but are not limited to, the following:

- There will be a number of reforms to the existing abstraction licensing regime (as provided for in the WRA). All new abstraction licences will be time-limited. From 2012, the right to compensation for revocation of an abstraction licence which causes significant environmental damage will be removed. The EA will have a new power to propose that one Regulated Company seeks a bulk supply from another, and to take a failure to do so into account in making licensing decisions;

- Regulated Companies will be under a new duty to prepare drought plans, to agree them with the Secretary of State and to make them publicly available;

- Regulated Companies will also be under a new duty to agree water resource management plans with the Secretary of State and to make them publicly available; and

- Regulated Companies’ licences can be amended so as to provide a new duty to further water conservation.

Competition in the Water Industry

The Competition Act

The Competition Act 1998 (the "Competition Act") introduced two prohibitions concerning anti-competitive agreements and conduct and powers of investigation and enforcement.

The Section I prohibition prohibits agreements between undertakings which may affect trade within the United Kingdom and which have as their object or effect the prevention, restriction or distortion of competition within the United Kingdom. The Chapter II prohibition prohibits the abuse of a dominant position which may affect trade within the United Kingdom.

The WSRA has concurrent powers with the OFT to apply and enforce the Competition Act to deal with anti-competitive agreements or abuses of dominance relating to the water and sewerage sector, including the power to enforce directions to bring an infringement to an end and to impose fines of up to 10 per cent. of worldwide group turnover of the Regulated Company involved, for the business year preceding the finding of the infringement, for infringing the Competition Act. Also, any arrangement which infringes the Competition Act may be void and unenforceable and may give rise to claims for damages from third parties.

Merger Regime

The OFT must refer to the CC a merger between two water enterprises (i.e. an enterprise carried on by a water or sewerage undertaking appointed under section 6 of the 1991 Water Act) unless either the value of the turnover of the target or the turnover of all water enterprises owned by the acquirer is below £10 million. The CC must then determine (i) whether arrangements are in progress which will result in a water merger or whether a water merger has taken place; (ii) if so, whether the merger may be expected to prejudice or has prejudiced the ability of the WSRA, in carrying out its duties under the WIA, to make comparisons between water enterprises; and (iii) if there is, or will be such a water merger and there is or will be such prejudice, whether to take action to remedy, mitigate or prevent the prejudice or any adverse effect resulting from it and, if so, what action should be taken. In taking any such action, the CC must have regard to the need to achieve as comprehensive a solution as is reasonable and practicable. It may take customer benefits into account in formulating remedies if they would not prevent the comprehensive solution or if they are substantially more important than the prejudice concerned. The CC's decision may be appealed to the Competition Appeal Tribunal by any person sufficiently affected by the decision.

In cases of an acquisition of a water enterprise by a company which is not already a water enterprise, general merger control rules apply. These may call for discussion with the OFT as well as Ofwat. The OFT (or the Secretary of State in some exceptional categories of case) has the power to investigate any merger within the jurisdiction of the UK merger regime and determine whether the transaction should be referred to the CC for further investigation to determine if the arrangement will or may be expected to substantially lessen competition in a market in the UK. The OFT will consult with Ofwat.

Depending on the size of the parties involved, mergers of two or more water enterprises and other mergers may require notification to the European Commission under the EU merger

regime (although the CC may still investigate the effect on the comparator principle in relation to mergers of two or more water enterprises).

Market Investigation Regime

Where it appears to the WSRA or the OFT (or the Secretary of State (acting alone or jointly with other Ministers) in some exceptional categories of case) that any feature(s) of the market(s) for water/sewerage or related services prevents, restricts or distorts competition for the supply of water/sewerage or related services, he/it may refer the matter to the CC. These powers relate to both structural and behavioural features. The CC will investigate the matter and, if such feature(s) exist(s) which have such an adverse effect on competition, the CC must consider what, if any, action should be taken to remedy or prevent them and may, if it thinks fit, order remedial action. The remedy may be implemented either by the giving of appropriate undertakings or by an order from the CC. The Secretary of State may also call for the consideration of wider public interest issues in certain other exceptional cases and may remedy any adverse effects in the public interest.

New Framework for Competition

To date, Regulated Companies have faced limited competition in the provision of water and sewerage services. This has primarily taken the form of:

- "inset appointments", which allow one Regulated Company to replace another as the statutory undertaker for a specified geographical area within the other Regulated Company's appointed area. "Inset competition" is available in respect of large users (customers using over 100 megalitres of water per annum in England, or 250 megalitres in Wales) or "greenfield" sites. As at 1 May 2005, Ofwat had made 11 inset appointments;

- competition in the trade effluent market, from customers (or their agents) who self-treat, in full or in part, their wastewater discharges, in order to reduce the charges they pay to their Regulated Company; and

- self-supply of raw water, usually by large industrial or agricultural undertakings who are located close to a river or other water source.

The Water Act provides new arrangements for competition for water supply. New licences will be granted to entrants who wish to:

- purchase "wholesale" water from Regulated Companies and sell it on to eligible customers; and

- input water in Regulated Companies' networks for supply to eligible customers, i.e. make use of common carriage services.

- Only customers using in excess of a threshold of 50 megalitres of water per annum will be eligible to switch to the new licensed suppliers ("Licensed Suppliers"). The threshold

may be altered by the Secretary of State by statutory instrument and the Government has signalled its intention to review the threshold within three years. Customers who use potable or non-potable water supplies above the threshold will be eligible to be supplied by Licensed Suppliers. SWS estimates that it has 61 of these customers, which together accounts for 5.2 per cent. of the water services turnover.

There are new duties on Regulated Companies to:

- provide a wholesale supply to Licensed Suppliers, subject to certain conditions; and

- allow Licensed Suppliers to input water into their networks, subject to certain conditions.

Where a Licensed Supplier disputes a Regulated Company's refusal to provide a wholesale supply or to allow water to be input into its network, it may refer the matter for determination to Ofwat.

Regulated Companies will be required to charge entrants for common carriage and wholesale services in such a way as to recover certain appropriate costs, to meet the Government's objective of minimising the effect of competition on other customers' bills.
A range of supporting provisions cover issues such as: drinking water quality regulation of Licensed Suppliers; the process for granting licences; enforcement of the duties of Licensed Suppliers; special administration arrangements for Licensed Suppliers; changes to the way in which Regulated Companies' supply duties apply outside their appointed area; and the imposition of various duties on Licensed Suppliers in connection with matters such as water efficiency and water conservation.

There are no equivalent proposals to introduce competition for sewerage services.

CHAPTER 7
SUMMARY OF THE FINANCING AGREEMENTS

Security Trust and Intercreditor Deed

General

The intercreditor arrangements in respect of the SWS Financing Group (the "**Intercreditor Arrangements**") are contained in the STID and the CTA. The Intercreditor Arrangements bind each of the Secured Creditors and each of the Obligors.

The Secured Creditors include the Class A Debt Providers, the Class B Debt Providers and the Mezzanine Facility Providers. Any new Authorised Credit Provider (or in respect of Bondholders, the Bond Trustee) will be required to accede to the STID and the CTA as a Class A Debt Provider, a Class B Debt Provider or a Mezzanine Facility Provider.

Unsecured creditors are not and will not become parties to the Intercreditor Arrangements and, although ranking behind the Secured Creditors in an administration or other enforcement, will have unfettered, independent rights of action in respect of their debts. However, the aggregate amount of unsecured Financial Indebtedness is restricted under the Common Terms Agreement.

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

The Intercreditor Arrangements provide for the ranking in point of payment of the claims of the Secured Creditors and for the subordination of all claims among the SWS Financing Group (other than claims in respect of the Issuer/SWS Loan Agreements funded through the raising of Class A Debt, Class B Debt and Mezzanine Debt).

Undertakings of Secured Creditors

Pursuant to the terms of the STID, each Secured Creditor (other than the Security Trustee) undertakes that it will not, except as expressly contemplated in the CTA, unless the Majority Creditors or, where applicable, the Super Majority Creditors otherwise agree:

(a) permit or require any Obligor to discharge any of the Secured Liabilities owed to it, save to the extent permitted by the STID, including (i) the Payment Priorities and (ii) in the case of the Mezzanine Debt and prepayments of other Financial Indebtedness (other than out of the proceeds of Permitted Financial Indebtedness) the Restricted Payment Condition;

(b) permit or require any Obligor to pay, prepay, repay, redeem, purchase, early or voluntarily terminate or otherwise acquire any of the Secured Liabilities owed to it, save

to the extent permitted by the CTA or the STID including pursuant to a Permitted Lease Termination or a Permitted Hedge Termination, pursuant to a provision for prepayment upon illegality or, in the case of Mezzanine Debt and prepayments of other Financial Indebtedness (other than out of the proceeds of Permitted Financial Indebtedness), if the Restricted Payment Condition is satisfied;

(c) take, accept or receive the benefit of any Security Interest, guarantee, indemnity or other assurance against financial loss from any of the Obligors in respect of any of the Secured Liabilities owed to it, except the Security and the Financial Guarantees or pursuant to the terms of the Finance Documents;

(d) take or receive from any of the Obligors by cash receipt, set-off, any right of combination of accounts or in any other manner whatsoever (other than set-off in relation to amounts in the Operating Accounts which are owed to the Account Bank or in relation to Standby Drawings owed to a Liquidity Facility Provider under a Liquidity Facility Agreement), the whole or any part of the Secured Liabilities owed to it, save to the extent permitted by the CTA or the STID; or

(e) except as described in "*Modifications, Consents and Waivers*" below, agree to any modification to, or consent or waiver under or in respect of, any term of any Finance Document to which it is a party.

Undertakings of Obligors

Pursuant to the terms of the STID, each Obligor undertakes that it will not, unless the Majority Creditors or, where applicable, the Super-Majority Creditors otherwise agree:

(i) discharge any of the Secured Liabilities owed by it, save to the extent contemplated in paragraph (a) of "*Undertakings of Secured Creditors*" above;

(ii) pay, prepay, repay, redeem, purchase, early or voluntarily terminate or otherwise acquire any of the Secured Liabilities owed by it, save to the extent contemplated in paragraph (b) of "*Undertakings of Secured Creditors*" above;

(iii) create or permit to subsist any Security Interest over any of its assets for, or any guarantee, indemnity or other assurance against financial loss in respect of, any of the Secured Liabilities owed by it, except the Security and the Financial Guarantees or pursuant to the terms of the Finance Documents;

(iv) (except as referred to in paragraph (d) of "*Undertakings of Secured Creditors*" above) discharge any of the Secured Liabilities by cash payment, set-off, any right of combination of accounts or in any other manner whatsoever, save to the extent permitted by the CTA or the STID;

(v) without the consent of the Security Trustee or, where applicable, each relevant Secured Creditor (as described in "*Modifications*, *Consents and Waivers*" below), agree to any modification to, or consent or waiver under or in respect of, any term of any Finance Document to which it is a party; or

(vi) take or omit to take any action whereby any subordination contemplated by the STID may be impaired.

Ranking of Secured Liabilities

The underlying principle of the Intercreditor Arrangements is that at all times the Class A Debt ranks in point of payment prior to any payment in respect of the Class B Debt and the Mezzanine Debt, the Class B Debt ranks in point of payment prior to the Mezzanine Debt and the Senior Mezzanine Debt ranks in point of payment prior to the Junior Mezzanine Debt (including in each case both prior to and during any Standstill Period, after acceleration of the Secured Liabilities and upon any enforcement of the Security), see Chapter 5 "*Risk Factors*" under "*Subordination of the Class B Bonds*" for further details. Prior to a Standstill Period payment dates for Class A Debt, Class B Debt and Mezzanine Debt may fall on different dates.

Modifications, Consents and Waivers

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

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

Class A Debt Instructing Group

Both prior to and during any Standstill Period, after acceleration of the Secured Liabilities and upon any enforcement of the Security prior to repayment in full of the Class A Debt, only the Qualifying Class A Debt Providers are eligible to exercise the rights of the Majority Creditors and, where appropriate, Super-Majority Creditors. Decisions of the Majority Creditors and, where applicable, Super-Majority Creditors will bind all of the Secured Creditors in all circumstances, save for certain Entrenched Rights and Reserved Matters that are fundamental to particular Secured Creditors (see "*Entrenched Rights and Reserved Matters*" below).

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

(a) in respect of each Sub-Class of Class A Wrapped Bonds or other Class A Wrapped Debt (if no FG Event of Default has occurred and is continuing in respect of the relevant Financial Guarantor), such Financial Guarantor;

(b) in respect of each Sub-Class of Class A Wrapped Bonds (after an FG Event of Default has occurred and is continuing in respect of the Financial Guarantor of those Class A Wrapped Bonds) and each Sub-Class of Class A Unwrapped Bonds, the Bond Trustee;

(c) in respect of the Initial RCF Agreement, the Initial RCF Agent, in respect of the Initial Term Facility, Artesian II and, in respect of the Second Artesian Term Facility, Financial Security Assurance (U.K.) Limited; and

(d) in respect of any other Secured Liabilities of the type referred to in paragraphs (a) to (c) above (excluding liabilities in respect of any Hedging Agreements or Liquidity Facilities) or (with the approval of the Majority Creditors) other types of Secured Liabilities that rank *pari passu* with all other Class A Debt, the relevant representative appointed under the terms of the relevant Finance Document and named in the STID or the relevant Accession Memorandum to the STID and the CTA as the Class A DIG Representative.

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

Unless a Default Situation has occurred and is continuing and no Emergency Instruction Notice has been served (see "*Emergency Instruction Procedure*" below), the Bond Trustee shall not be entitled to convene a meeting of any Series, Class or Sub-Class of Bonds to consider any proposal to be voted on by the Class A DIG except where such proposal is the subject of an Entrenched Right or a Reserved Matter in respect of such Series, Class or Sub-Class.

Decisions of the Majority Creditors and, where appropriate, Super-Majority Creditors will be determined by votes on a pound for pound basis (based on the Outstanding Principal Amount of the Qualifying Class A Debt voted by the Class A DIG Representatives). Subject to Entrenched Rights and Reserved Matters, the Security Trustee will be entitled to act on the instructions of the Majority Creditors or, as the case may be, Super-Majority Creditors of those Class A DIG Representatives which have actually voted by the specified date for voting, which date must be not less than 10 business days (or in certain circumstances five business days) after the date the STID Directions Request is deemed to be given (or, where the Bond Trustee is a DIG Representative and a Default Situation is continuing (subject to the Emergency Instruction Procedure — see "*Emergency Instruction Procedure*" below), such later date (not later than two months after such date) as is requested of the Security Trustee by the Bond Trustee should the Bond Trustee consider it necessary to convene a meeting of any one or more Series, Class or Sub-Class of Bondholders to seek directions) or, if earlier, as soon as Class A DIG Representatives in respect of more than 50 per cent. (or 66⅔ per cent. for Super-Majority Creditor decisions) of the Qualifying Class A Debt have voted in favour of the relevant proposal.

Class B Debt Instructing Group

Following repayment in full of the Class A Debt, the Qualifying Class B Debt Providers will be eligible to exercise the rights of the Majority Creditors and, where appropriate, Super-Majority Creditors. After repayment in full of the Class A Debt, decisions of such Majority Creditors or, as the case may be, Super-Majority Creditors will bind all of the Secured Creditors in all

circumstances, save for certain Entrenched Rights and Reserved Matters that are fundamental to particular Secured Creditors. See "*Entrenched Rights and Reserved Matters*" below.

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

(a) in respect of each Sub-Class of Class B Wrapped Bonds (if no FG Event of Default has occurred and is continuing in respect of the relevant Financial Guarantor), such Financial Guarantor;

(b) in respect of each Sub-Class of Class B Wrapped Bonds (after an FG Event of Default has occurred and is continuing in respect of the Financial Guarantor of those Class B Wrapped Bonds) and each Sub-Class of Class B Unwrapped Bonds, the Bond Trustee; and

(c) in respect of any other Secured Liabilities of the type referred to in paragraphs (a) and (b) above (excluding liabilities in respect of any Currency Hedging Agreements in relation to Class B Debt) or (with the approval of the Majority Creditors) other types of Secured Liabilities that rank *pari passu* with all other Class B Debt, the relevant representative appointed under the terms of the relevant Finance Document and named in the relevant Accession Memorandum to the STID as the Class B DIG Representative.

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

Unless a Default Situation has occurred and no Emergency Instruction Notice has been served (see "*Emergency Instruction Procedure*" below) and is continuing, the Bond Trustee is not entitled to convene a meeting of any Series, Class or Sub-Class of Bonds to consider any proposal to be voted on by the Class B DIG except where such proposal is the subject of an Entrenched Right or a Reserved Matter in respect of such Series, Class or Sub-Class.

Decisions of the Majority Creditors and, where appropriate, Super-Majority Creditors will be determined by votes on a pound for pound basis (based on the Outstanding Principal Amount of the Qualifying Class B Debt voted by the Class B DIG Representatives). Subject to Entrenched Rights and Reserved Matters, the Security Trustee will be entitled to act on the instructions of the Majority Creditors or, as the case may be, Super-Majority Creditors of those Class B DIG Representatives which have actually voted by the specified date for voting, which date must be not less than 10 business days (or in certain circumstances five business days) after the date the STID Directions Request is deemed to be given (or, where the Bond Trustee is a DIG Representative and a Default Situation is continuing (subject to the Emergency Instruction Procedure — see "*Emergency Instruction Procedure*" below), such later date (not later than two months after such date) as is requested of the Security Trustee by the Bond Trustee should the Bond Trustee consider it necessary to convene a meeting of any one or more Series, Class or Sub-Class of Bondholders to seek directions) or, if earlier, as soon as Class B DIG

Representatives in respect of more than 50 per cent. (or 66⅔ per cent. for Super-Majority Creditor decisions) of the Qualifying Class B Debt have voted in favour of the relevant proposal.

Senior Mezzanine and Junior Mezzanine Debt Instructing Groups

Following repayment in full of the Class A Debt and the Class B Debt, the Senior Mezzanine Debt Providers will be eligible to exercise the rights of the Majority Creditors and, where appropriate, the Super-Majority Creditors. Following repayment in full of the Class A Debt, the Class B Debt and the Senior Mezzanine Debt, the Junior Mezzanine Debt Providers will be eligible to exercise the rights of the Majority Creditors and, where appropriate, Super-Majority Creditors.

Voting by the Bond Trustee as DIG Representative of the Bondholders

Where the Bond Trustee acts as the DIG Representative of some or all of the Wrapped Bondholders (following the occurrence of an FG Event of Default which is continuing in respect of the relevant Financial Guarantor of those Wrapped Bonds) and/or the Unwrapped Bondholders, the Bond Trustee may, both prior to a Default Situation and/or whilst a Default Situation is continuing, in its absolute discretion, vote on a STID Proposal or a DIG Proposal (without reference to any Bondholders) in respect of the aggregate Outstanding Principal Amount of some or all of such Sub-Classes of Bonds, but shall not, prior to a Default Situation, be entitled to convene a meeting of any Series, Class or Sub-Class of Bondholders to seek directions (except in respect of an Entrenched Right or Reserved Matter of such Series, Class or Sub-Class of Bondholders).

Additionally whilst a Default Situation is continuing, where the Bond Trustee acts as the DIG Representative in respect of Bonds, the Bond Trustee shall not be entitled to convene a meeting of the Bondholders to direct the Security Trustee in accordance with an extraordinary resolution of the relevant Sub-Class of Bonds after the presentation of a valid Emergency Instruction Notice pursuant to the terms of the STID. See "*Emergency Instruction Procedure*" below.

Emergency Instruction Procedure

Whilst a Default Situation is subsisting, certain decisions and instructions may be required in a timeframe which does not allow the Bond Trustee to convene Bondholder meetings. To cater for such circumstances, the Intercreditor Arrangements provide for an emergency instruction procedure (the "**Emergency Instruction Procedure**") which is subject to Entrenched Rights and Reserved Matters. The Security Trustee will be required to act upon instructions contained in an emergency instruction notice (an "**Emergency Instruction Notice**"). An Emergency Instruction Notice must be signed by DIG Representatives (the "**EIN Signatories**") representing 66⅔ per cent. or more of the aggregate Outstanding Principal Amount of the Qualifying Class A Debt (or following the repayment in full of the Class A Debt, the Qualifying Class B Debt) after excluding the proportion of Qualifying Debt in respect of which the Bond Trustee is the DIG Representative and in respect of which the Bond Trustee in its absolute discretion has not voted. The Emergency Instruction Notice must specify the emergency action which the Security Trustee is being instructed to take and must certify that in the EIN Signatories' reasonable opinion,

unless such action is taken within the timeframe specified in the Emergency Instruction Notice, the interests of the EIN Signatories would be materially prejudiced.

Hedge Counterparties

Each Hedge Counterparty is or will be a Secured Creditor party to the STID and the CTA and each Hedging Agreement to hedge the currency of any Class A Debt or to hedge interest rates constitutes or will constitute Class A Debt or, if entered into to hedge the currency of any Class B Debt, Class B Debt.

The Hedge Counterparties will not form part of the Class A DIG or, in the case of any Currency Hedging Agreement in relation to Class B Debt, the Class B DIG However, except in relation to certain amounts payable by the Issuer under any Currency Hedging Agreement in relation to Class B Debt, all fees, interest and principal payable by the Issuer to the Hedge Counterparties will rank in the Payment Priorities senior to or *pari passu* with interest or principal payments on the Class A Bonds. See "*Cash Management*" and "*Hedging Agreements*" below.

Liquidity Facility Providers

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

The Liquidity Facility Providers will not form part of the Class A DIG. However, fees, interest and principal of the Liquidity Facility Providers will rank in the Payment Priorities senior to interest and principal payments on the Class A Bonds. See "*Cash Management*" and "*The Liquidity Facilities*" below.

Finance Lessors

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

Amounts due and payable under the Finance Leases are dealt with in "*Cash Management*" below.

Standstill

The STID provides for an automatic standstill of the claims of the Secured Creditors against SWS and the Issuer (the "**Standstill**") immediately following notification to the Security Trustee of an Event of Default (other than an Event of Default under any Hedging Agreement with respect to a Hedge Counterparty under such Hedging Agreement) and for so long as any Class A Debt and/or Class B Debt is outstanding.

The Standstill is designed to reduce or postpone the likelihood of a Special Administration Order being made against SWS on the grounds of its insolvency or otherwise. Although not binding on unsecured and trade creditors and hence potentially giving such unsecured and trade creditors a position of greater strength upon an Event of Default, it is intended to enable SWS to continue as a going concern and to allow time for the financial condition of SWS to be restored.

During the Standstill Period:

(a) none of the Secured Creditors will be entitled to give any instructions to the Security Trustee to take any Enforcement Action (but without prejudice to the ability of the Secured Creditors to demand payment) in relation to the Security granted by the Issuer or SWS;

(b) the Security granted by SWSGH and SWSH may be enforced at any time by the Security Trustee at the direction of the Majority Creditors except in the case of a Standstill Period which has commenced as a result of the occurrence of the Event of Default pursuant to a rating downgrade of the Bonds (no other Event of Default having occurred and being outstanding), in which case such Security may only be enforced at any time following the date which is three months from the date of commencement of the Standstill Period provided that such Event of Default is continuing at such time;

(c) save as provided in paragraphs (a) and (b) above, no Enforcement Action may be taken by any Secured Creditor; and

(d) any monies received by SWS or the Issuer will be applied in accordance with the cash management provisions contained in the CTA (see "*Cash Management*" below) and in accordance with the Payments Priorities (see "*Cash Management — Debt Service Payment Account*" below).

Notwithstanding the Standstill, the Secured Creditors will be entitled to accelerate their claims to the extent required to apply proceeds of enforcement of the Share Pledges provided by SWSH and SWSGH under the Security Documents.

The period of the Standstill in respect of any Event of Default relating to SWS and/or the Issuer (the "**Standstill Period**") will be 18 months unless the Standstill Period is extended beyond 18 months (see "*Standstill Extension*" below) or any of the following occur prior to the expiry of the relevant Standstill Period:

(a) an order is made for the Special Administration of SWS or any steps are taken to commence insolvency proceedings against the Issuer or SWS other than proceedings that are commenced by the Security Trustee;

(b) (during the first 18 months of the Standstill Period) Class A DIG Representatives in respect of 66⅔ per cent. or more of the aggregate Outstanding Principal Amount of the Qualifying Class A Debt or (following the repayment in full of the Class A Debt) Class B DIG Representatives in respect of 66⅔ per cent. or more of the aggregate Outstanding Principal Amount of the Qualifying Class B Debt vote to terminate the Standstill Period and (after the first 18 months) the date on which the Standstill Period terminates (see "*Standstill Extension*" below);

(c) the waiver or remedy of the relevant Event of Default giving rise to the Standstill Period; or

(d) the Security Trustee notifies SWS and each Secured Creditor (or its DIG Representative) that notice by any Secured Creditor of the occurrence of the relevant Event of Default has been revoked.

The occurrence of a Standstill will not of itself prevent the Issuer drawing under the Liquidity Facilities.

Upon termination of a Standstill Period (except by virtue of the matters referred to in paragraphs (c) and (d) above), each Secured Creditor will be entitled to exercise all rights which may be available to it under any Finance Document to which it is a party (other than any Security Document) including directing the Security Trustee to take Enforcement Action.

Standstill Extension

The Standstill Period shall automatically be extended beyond 18 months:

(a) for a further 120 days unless Class A DIG Representatives in respect of 50 per cent. or more of the aggregate Outstanding Principal Amount of Qualifying Class A Debt vote at any time prior to or during such further 120 days to terminate the Standstill Period;

(b) following the period referred to in paragraph (a) above, for a further 60 days unless Class A DIG Representatives in respect of 33⅓ per cent. or more of the aggregate Outstanding Principal Amount of Qualifying Class A Debt vote at any time prior to or during such further 60 days to terminate the Standstill Period; and

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

The Bond Trustee shall not form part of the Class A DIG in respect of any vote to terminate the Standstill Period, unless directed or requested to vote in such manner (i) by an Extraordinary Resolution of the relevant Sub-Class of Class A Wrapped Bonds (following the occurrence of an FG Event of Default which is continuing in respect of the relevant Financial Guarantor of such Sub-Class of Class A Wrapped Bonds) or Class A Unwrapped Bonds or (ii) in writing by Bondholders holding not less than 25 per cent. of the Outstanding Principal Amount of the relevant Sub-Class of Class A Bonds.

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

The period of Standstill in respect of any Event of Default other than an Event of Default relating to SWS and/or the Issuer will terminate upon the earlier of (a) the date of the waiver or remedy of the relevant Event of Default giving rise to the Standstill Period and (b) the date on which the

Security Trustee notifies SWS and each Secured Creditor (or its DIG Representative) that notice by any Secured Creditor of the occurrence of the relevant Event of Default has been revoked.

Enforcement

Following an Event of Default and for so long as it is continuing, the Majority Creditors may direct the Security Trustee to enforce the Security created by SWSGH and SWSH; following the termination of a Standstill Period (except under paragraph (c) or (d) of "*Standstill*" above), the Majority Creditors may direct the Security Trustee to enforce the Security created by SWS and the Issuer.

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

The holders of the SWS Preference Shares and the Mezzanine Facility Providers are subject to certain call option arrangements under which they will be required (subject to certain conditions) to sell their SWS Preference Shares (other than the Class A2 Preference Shares) or, as the case may be, their Mezzanine Debt in the event that the Security Trustee or any receiver appointed by it sells the ordinary shares in SWSH or SWS following the enforcement of the Security created by SWSGH or SWSH. In this event, the holders of the SWS Preference Shares will be required to sell their shares (other than the Class A2 Preference Shares) to the person that acquires the ordinary shares in SWSH or SWS on an enforcement of the Security created by SWSGH or SWSH (or to any nominee of such person) for a price to be determined in accordance with the SWS Preference Share Deed (see "*SWS Preference Shares*" below) and the Mezzanine Facility Providers will be required, if any of their Mezzanine Debt remains outstanding following the application of the proceeds of such enforcement of Security pursuant to the Payment Priorities, to sell their debt at its market value (likely to be a nominal amount). The rights of the holders of the Class A2 Preference Shares shall be deferred upon any sale of the other SWS Preference Shares pursuant to these call option arrangements.

Excluded Accounts

Although the Issuer has pursuant to the Security Agreement created first fixed charges over the Excluded Accounts in favour of the Security Trustee, the Security Documents provide that, on and following an Acceleration of Liabilities (other than a Permitted Lease Termination, Permitted Hedge Termination or Permitted Share Pledge Acceleration), all monies held in the Issuer's O&M Reserve Account and the Debt Service Reserve Account will be held by the Security Trustee on trust for the relevant Liquidity Facility Providers whose commitments have been drawn to fund the Issuer's O&M Reserve Account or, as the case may be, the Debt Service Reserve Account and in the proportions that their respective drawn amounts under the relevant O&M Reserve Facility Agreement or, as the case may be, DSR Liquidity Facility Agreement bear to the balance on the O&M Reserve Account or, as the case may be, the Debt Service Reserve Account.

Accession of Additional Secured Creditors

The STID requires that, to the extent that SWS and/or the Issuer wishes any Authorised Credit Provider (or, in respect of Bonds, its Secured Creditor Representative) or other person to obtain the benefit of the Security, such Authorised Credit Provider or other person (other than Bondholders) must sign an Accession Memorandum whereby it agrees to be bound by the terms of the STID and the CTA, including those provisions which prohibit individual Secured Creditors from taking action without the consent of the Majority Creditors or, where appropriate, the Super-Majority Creditors. Holders of SWS Preference Shares who, by virtue of the terms of the SWS Preference Shares, become holders of Subordinated Debt upon the conversion of the SWS Preference Shares into Subordinated Debt may elect to accede to (or cause its trustee to accede to) the terms of the STID and the CTA as a Secured Creditor for the reasons described immediately above.

Activities of the Security Trustee

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

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

Super-Majority Creditor Decisions

Whilst most of the decisions relating to any waiver, consent or modification under or in respect of a Finance Document require the approval of the Majority Creditors (subject always to the Entrenched Rights and Reserved Matters of Secured Creditors), the STID provides that a limited number of decisions (relating to the ability of the Obligors to raise further Financial Indebtedness or create Security Interests) require the approval of the Super-Majority Creditors.

Entrenched Rights and Reserved Matters

Modifications, consents and waivers will be agreed by the Security Trustee, in accordance with votes of the Majority Creditors or, where appropriate, Super-Majority Creditors, subject to Entrenched Rights and Reserved Matters. Such modifications, consents and waivers will be binding on all of the Secured Creditors, subject to Entrenched Rights and Reserved Matters. No Entrenched Right or Reserved Matter will operate to override the provisions contained in the CTA which allow SWS (following a Periodic Review or as a result of any material change in the regulation of the water industry in the United Kingdom) to amend any financial ratio contained within the covenants, Trigger Events or Events of Default provided that each Financial Guarantor and the Security Trustee (acting on the instructions of the Majority Creditors) agree and the relevant ratings set out in definition of Rating Requirement (in relation to the Class A Bonds) and the ratings ascribed to the Class B Bonds at the time of their issue have been

affirmed by all Rating Agencies then rating the Class A Bonds and/or the Class B Bonds as applicable.

Lists of Entrenched Rights and Reserved Matters are contained in "*Entrenched Rights*" and "*Reserved Matters*", below.

Entrenched Rights

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

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

(a) the relevant Class A Debt Provider (or, where applicable, its Secured Creditor Representative) has demonstrated to the satisfaction of the Security Trustee would increase or adversely modify its obligations or liabilities under or in connection with the STID or any other Finance Document;

(b) (i) would release any of the Security (unless equivalent replacement security is taken at the same time) unless such release is permitted in accordance with the terms of the STID and the relevant Security Document or (ii) would alter the rights of priority of, or the enforcement by, the relevant Class A Debt Provider (or, where applicable, its Secured Creditor Representative) under the Security Documents other than as expressly contemplated therein;

(c) would change or would relate to the Payment Priorities;

(d) would change or would relate to the Entrenched Rights or the Reserved Matters or, where applicable, the relevant Class A Debt Provider's Entrenched Rights or Reserved Matters;

(e) would change or would relate to (i) the definitions of "Class A DIG", "Class A DIG Representatives", "DIG Proposal", "DIG Directions Request", "Majority Creditors", "Restricted Payment", "Restricted Payment Condition", "Qualifying Class A Debt", "Super-Majority Creditors" or "Voted Qualifying Class A Debt", (ii) those matters expressly requiring the consent, approval or agreement of, or directions or instructions from, or waiver by the Majority Creditors, Super-Majority Creditors or the Security Trustee or (iii) the percentages of aggregate Outstanding Principal Amount of Qualifying Class A Debt required to terminate a Standstill;

(f) would delay the date fixed for payment of principal, interest or Make-Whole Amount in respect of the relevant Class A Debt Provider's Class A Debt or of any fees or premia in respect thereof or would reduce the amount of principal, interest or Make-Whole Amount payable in respect of such Class A Debt or the amount of any fees or premia in respect thereof;

(g) would bring forward the date fixed for payment of principal, interest or Make-Whole Amount in respect of Class A Debt or Class B Debt or any fees or premia in respect thereof or would increase the amount of principal, interest or Make-Whole Amount payable on any date in respect of Class A Debt or Class B Debt or any fees or premia in respect thereof;

(h) would result in the exchange of the relevant Class A Debt Provider's Class A Debt for, or the conversion of such Class A Debt into, shares, bonds or other obligations of any other person;

(i) would change or would relate to the currency of payment due under the relevant Class A Debt Provider's Class A Debt (other than due to the United Kingdom joining the euro);

(j) (subject to paragraph (k) below) would change any Event of Default or any Trigger Event relating to financial ratios or credit rating downgrade;

(k) would relate to the waiver of the non-payment Event of Default in respect of any Obligor or Events of Default or Trigger Events relating to non-payment, credit rating downgrade or financial ratios or the making of Restricted Payments (see "*Common Terms Agreement*" under "*Trigger Events*" and "*Events of Default*" below);

(l) would change or would relate to the rights of the relevant Class A Debt Provider to receive any sums owing to it for its own account in respect of premia, fees, costs, charges, liabilities, Taxes, damages, proceedings, claims and demands in relation to any Finance Document to which it is a party (excluding, for the avoidance of doubt, the principal, interest or Make-Whole Amount payable to the relevant Class A Debt Provider); or

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

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

(a) the relevant Class B Debt Provider (or, where applicable, its Secured Creditor Representative) has demonstrated to the satisfaction of the Security Trustee would increase or adversely modify its obligations or liabilities under or in connection with the STID or any other Finance Document;

(b) (i) would release any of the Security (unless equivalent replacement security is taken at the same time) unless such release is permitted in accordance with the terms of the STID and the relevant Security Document or (ii) would alter the rights of priority of or the enforcement by the relevant Class B Debt Provider (or, where applicable, its Secured

Creditor Representative) under the Security Documents other than as expressly contemplated therein;

(c) would change or would relate to the Payment Priorities;

(d) would change or would relate to the Entrenched Rights or the Reserved Matters or, where applicable, the relevant Class B Debt Provider's Entrenched Rights or Reserved Matters;

(e) would change or would relate to (i) the definitions of "Class B DIG", "Class B DIG Representatives", "DIG Proposal", "DIG Directions Request", "Majority Creditors", "Restricted Payment", "Restricted Payment Condition", "Super-Majority Creditors", "Qualifying Class B Debt" or "Voted Qualifying Class B Debt", (ii) those matters expressly requiring the consent, approval or agreement of, or directions or instructions from, or waiver by the Majority Creditors or the Security Trustee or (iii) the percentages of aggregate Outstanding Principal Amount of Qualifying Class B Debt required to terminate a Standstill;

(f) would delay the date fixed for payment of principal, interest or Make-Whole Amount in respect of the relevant Class B Debt Provider's Class B Debt or any fees or premia in respect thereof or would reduce the amount of principal, interest or Make-Whole Amount payable on any date in respect of such Class B Debt or any fees or premia in respect thereof;

(g) would bring forward the date fixed for payment of principal, interest or Make-Whole Amount in respect of Class A Debt or Class B Debt or any fees or premia in respect thereof or would increase the amount of principal, interest or Make-Whole Amount payable on any date in respect of Class A Debt or Class B Debt or any fees or premia in respect thereof;

(h) would result in the exchange of the relevant Class B Debt Provider's Class B Debt for, or the conversion of such Class B Debt into, shares, bonds or other obligations of any other person;

(i) would change or would relate to the currency of payment under the relevant Class B Debt Provider's Class B Debt (other than due to the United Kingdom joining the euro);

(j) (subject to paragraph (k) below) would change any Event of Default or any Trigger Event relating to financial ratios or credit rating downgrade;

(k) would relate to the waiver of the non-payment Event of Default in respect of any Obligor or Events of Default or Trigger Events relating to non-payment, credit rating downgrade or financial ratios or the making of Restricted Payments (see "*Common Terms Agreement*" under "*Trigger Events*" and "*Events of Default*" below);

(l) would change or would relate to the rights of the relevant Class B Debt Provider to receive any sums owing to it for its own account in respect of premia, fees, costs, charges, liabilities, Taxes, damages, proceedings, claims and demands in relation to any Finance Document to which it is a party (excluding, for the avoidance of doubt, the

principal, interest or Make-Whole Amount payable to the relevant Class B Debt Provider); or

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

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

(a) any sale, transfer or other disposal (whether deemed or otherwise) of any of the Equipment;

(b) the affixing of any Equipment to any land or building to which SWS or the Issuer (as applicable) does not have an interest in such land for the purposes of the Capital Allowances Act 2001;

(c) the creation or subsistence of any encumbrance, lien, mortgage or other Security Interest over any Equipment;

(d) any of the covenants or representations and warranties set out in the Finance Documents which relate to the maintenance or condition of the Equipment;

(e) any provision(s) contained in the Finance Documents pertaining to any damage, destruction or total loss of any of the Equipment;

(f) any elections filed with HM Revenue and Customs by SWS or the Issuer (as applicable) and any Finance Lessor under the Finance Leases pursuant to Sections 177 and/or 227 of the Capital Allowances Act 2001 in respect of the Equipment and the relevant Finance Lessor's expenditure on the Equipment;

(g) the provisions relating to the calculation of rental payments and/or sums due upon termination of the leasing of any Equipment; and

(h) any changes to the Entrenched Rights of the Finance Lessors set out in paragraphs (a) to (g) above.

Entrenched Rights of the Mezzanine Facility Providers

The Mezzanine Facility Providers enjoy some of the same Entrenched Rights as apply to the Class B Debt Providers insofar as is necessary to protect the fundamental terms of their investment. In addition:

(a) for so long as no Default has occurred and is continuing, no modification can be made which would have the effect of changing or supplementing any of the provisions contained in Paragraph 37 (*Restricted Payments*) of Part 3 of Schedule 5 (*Covenants*) to the Common Terms Agreement; any of the Trigger Events contained in Part 1 of

Schedule 6 (*Trigger Events*) to the Common Terms Agreement; any of the remedies to Trigger Events contained in Part 3 of Schedule 6 (*Trigger Events*) to the Common Terms Agreement; or any of the Events of Default set out in Schedule 7 (*Events of Default*) to the Common Terms Agreement, in each case where the effect of such change or supplement would or might reasonably be expected to be adverse to the interests of a Mezzanine Facility Provider; or

(b) unless and until (i) an Event of Default has occurred and is continuing or (ii) a Trigger Event has occurred and is continuing and a Remedial Plan has concluded that the failure to raise new Financial Indebtedness would or could reasonably be expected to lead to an Event of Default and provided that the Security Trustee has received an Entrenched Rights or Reserved Matters Notice from any Mezzanine Facility Provider (or its Secured Creditor Representative), no modification to, or consent or waiver under or in respect of, any term of the STID and/or any other Finance Document will be effective if the proposed modification, consent or waiver would permit the raising of new Financial Indebtedness by the SWS Financing Group to the extent that, as a result, the aggregate of the Senior Net Indebtedness and any other net indebtedness ranking in point of priority senior to the Senior Mezzanine Debt would exceed 90 per cent. of RCV,

unless the Security Trustee has received written consent to such modification, consent or waiver from at least 66⅔ percent by value of Mezzanine Facility Providers of each of the Senior Mezzanine Facility and the Junior Mezzanine Facility (or from their Secured Creditor Representatives).

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

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

Reserved Matters

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

Those Reserved Matters which each Secured Creditor reserves to itself to decide are each and every right, power, authority and discretion of, or exercisable by, each-such Secured Creditor at any time:

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

(b) to make determinations of and require the making of payments due and payable to it under the provisions of the Authorised Credit Facilities to which it is a party (as permitted under the CTA);

(c) to exercise the rights vested in it or permitted to be exercised by it under and pursuant to the CTA and the STID;

(d) to receive notices, certificates, communications or other documents or information under the Finance Documents or otherwise;

(e) to assign its rights or transfer any of its rights and obligations under any Authorised Credit Facility subject always to the requirement of the assignee or transferee to accede to the CTA and the STID as a Secured Creditor;

(f) in the case of each Finance Lessor, to inspect the relevant Equipment, to make calculations under the financial schedules to the relevant Finance Lease (or the equivalent provisions thereunder relating to the calculation of Rental or termination sums) and to terminate the relevant Finance Lease provided such termination is a Permitted Lease Termination;

(g) in the case of each Hedge Counterparty, to terminate the relevant Hedging Agreement provided such termination is a Permitted Hedge Termination; and

(h) in the case of any Secured Creditor, to accelerate their claims, to the extent necessary to apply proceeds of enforcement of the Share Pledges provided by SWSGH and SWSH pursuant to the terms of the Security Documents.

The Bond Trustee, the Security Trustee, the Mezzanine Facility Lenders, the Hedge Counterparties and the Financial Guarantors each have certain additional Reserved Matters which each has reserved to itself to decide. For the Bond Trustee and each Financial Guarantor, these include rights vested in it pursuant to the terms of the Bond Trust Deed and the Financial Guarantee. For the Security Trustee, these include rights vested in it pursuant to the terms of the STID.

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

(i) to make any determination contemplated or required under the Bond Trust Deed as to the occurrence or otherwise of an FG Event of Default, in relation to its Reserved Matters and in relation to its Entrenched Rights;

(ii) to agree to make any amendment or any waiver or consent which has the effect of resulting in or permitting any amendment to the provisions of any Financial Guarantee;

(iii) to make any claim under, or enforce any provision of, any Financial Guarantee;

(iv) which is provided for the purpose of enabling the Bond Trustee to protect its own position and interests in its personal capacity (including its own personal financial interests) or which the Bond Trustee determines to be necessary or appropriate to exercise for the protection of its own position and interests in its personal capacity;

(v) to determine amounts due in relation to and to claim under indemnities in favour of the Bond Trustee in its own capacity or for and on behalf of Bondholders under the Finance Documents;

(vi) to receive any amounts owing to it for its own account in accordance with the provisions of the Finance Documents;

(vii) to determine the amount of sums due in relation to expenses and stamp duties pursuant to the Finance Documents;

(viii) to make a claim for expenses under the Finance Documents;

(ix) to receive notices, certificates, communications or other documents or information under the Finance Documents or otherwise;

(x) which relieves or exempts the Bond Trustee from liability and exculpates or exonerates it (including, without limitation, any right of the Bond Trustee under any of the Finance Documents to make assumptions as to, or rely on any notice, certificate or other communication confirming, the existence or non-existence of any act, circumstance or event);

(xi) against or in relation to the relevant Bondholders;

(xii) under the Fourth Schedule (*Provisions for Meetings of Bondholders*) of the Bond Trust Deed;

(xiii) the right to appoint a co-trustee or to retire under, as the case may be, Clause 24 (*New Bond Trustee*) and Clause 25 (*Bond Trustee's Retirement and Removal*) of the Bond Trust Deed;

(xiv) the publication of an Interest Rate or Interest Amount, as the case may be, in accordance with Condition 6(h) (*Determination and Publication of Interest Rates, Interest Amounts, Redemption Amounts and Instalment Amounts*);

(xv) the determination of amounts in accordance with Condition 6(h) (*Determination and Publication of Interest Rates, Interest Amounts, Redemption Amounts and Instalment Amounts*);

(xvi) the selection of or made by an Indexation Adviser in accordance with Condition 7(a) (*Definitions*) and 7(c)(ii) (*Changes in Circumstances Affecting the Index – Delay in publication of Index*);

(xvii) the consideration and approval in relation to a substitute index figure in accordance with Conditions 7(e)(i) to (iii) inclusive (*Cessation of or Fundamental Changes to the Index*);

(xviii) the variation, termination and appointment of Agents in accordance with Condition 9(e) (*Appointment of the Agents*); and

(xix) to consent to any proposed amendment to, as the case may be, the Bond Trust Deed, the relevant Conditions or any Finance Document to which it is a party whether such consent is sought to correct a manifest error or is of a formal, minor or technical nature (and, for the avoidance of doubt, any other matter referred to in Clause 19 (*Modification, Consent and Waiver*) of the Bond Trust Deed will be subject to the directions of the Majority Creditors).

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

(a) the publication of an Interest Rate or Interest Amount in accordance with Condition 6(h) (*Determination and Publication of Interest Rates, Interest Amounts, Redemption Amounts and Instalment Amounts*);

(b) the determination of amounts in accordance with Condition 6(h) (*Determination and Publication of Interest Rates, Interest Amounts, Redemption Amounts and Instalment Amounts*);

(c) the selection of or made by an Indexation Adviser in accordance with Condition 7(a) (*Definitions*) and 7(c)(ii) (*Changes in Circumstances Affecting the Index — Delay in publication of the Index*);

(d) the consideration and approval in relation to a substitute index figure in accordance with Condition 7(e)(i) to (iii) inclusive (*Cessation of or Fundamental Changes to the Index*); and

(e) the variation, termination and appointment of Agents in accordance with Condition 9(e) (*Appointment of the Agents).*

Each Financial Guarantor of Wrapped Debt (other than Wrapped Bonds) has and will have similar matters reserved to it in respect of the determination of interest, interest amounts and repayment amounts, the selection of an indexation adviser, approval of substitute index figure, variation, termination and appointment of Agents under the Authorised Credit Facility under which such Wrapped Debt is incurred by SWS or the Issuer in addition to any amendment to Part C (Financial Guarantor Reserved Matters) of Schedule 3 to the STID.

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

(i) pursuant to the STID;

(ii) to receive any sums owing to it for its own account in respect of fees, costs, charges, liabilities, damages, proceedings, claims and demands in performing its powers and exercising its discretions under the STID and any other Finance Document to which the Security Trustee is a party;

(iii) which is provided for the purpose of enabling the Security Trustee to protect its own position and interests in its personal capacity (including its own personal financial interest) or which the Security Trustee determines to be necessary or appropriate to exercise for the protection of its own position and interests in its personal capacity;

(iv) except as otherwise specifically provided in the STID, to apply any of the sums referred to in Clause 15 (*Activities of the Security Trustee*) of the STID in accordance with such Clause;

(v) to receive notices, certificates, communications or other documents or information, to direct that such notices, certificates, communications or other documents or information must be provided (or must not be provided) to it or (subject to the disclosure of information provisions of the CTA) any other party, or, where applicable, to determine the form and content of any notice, certificate, communication or other document;

(vi) which relieves or exempts the Security Trustee from liability or exculpates or exonerates it (including, without limitation, any right of the Security Trustee under any of the Finance Documents to make assumptions as to, or rely on any notice, certificate or other communication confirming, the existence or non-existence of any act, circumstance or event);

(vii) to determine amounts due in relation to and to claim under indemnities in favour of the Security Trustee under Clause 15.5 (*Indemnification of the Security Trustee*) or Clause 16 (*Remuneration and Indemnification of the Security Trustee*) of the STID or pursuant to any other Finance Documents;

(viii) to appoint a co-trustee or to retire under Clause 17 (*Appointment of Additional Trustees*) and Clause 19.6 (*Resignation of the Security Trustee*) of the STID; and

(ix) to agree modifications to, or give any consent or grant any waiver under or in respect of, any term of the STID or any other Finance Document to which the Security Trustee is a party or over which it has Security under the Security Documents in accordance with Clause 8.2 (*Procedures for Modifications, Consents and Waivers*) of the STID.

Substitution of the Issuer

The Security Trustee shall implement any STID Proposal proposing the substitution in place of the Issuer, or any substituted Issuer, as the principal debtor under the Finance Documents of any other company incorporated in any other jurisdiction meeting the criteria for such a single purpose company established from time to time by the Rating Agencies. The implementation of any such proposal is an Entrenched Right of the Bond Trustee and each Financial Guarantor.

Intercompany Loan Arrangements

Issuer/SWS Loan Agreements

All Financial Indebtedness raised by the Issuer from time to time (whether through the issue of Bonds or raising of debt under Authorised Credit Facilities) is and will be backed by an aggregate matching debt obligation owed by SWS to the Issuer under a loan agreement (each an "**Issuer/SWS Loan Agreement**"). As such, the Issuer/SWS Loan Agreements are a source of funds capable of servicing any payments due and payable on the Bonds.

In the case of the initial Issuer/SWS Loan Agreement entered into on the Initial Issue Date (the "**Initial Issuer/SWS Loan**"), the aggregate nominal amount of all Financial Indebtedness raised through the issue of Bonds and the raising of Mezzanine Debt and the Initial Term Facility on the Initial Issue Date was lent by the Issuer to SWS under the Initial Issuer/SWS Loan Agreement on the Initial Issue Date. Each advance under the Initial Issuer/SWS Loan Agreement corresponds to the principal amount of the relevant Sub-Class of Bonds issued on the Initial Issue Date, the principal amount of the Senior Mezzanine Debt and the Junior Mezzanine Debt or, as the case may be, other debt under the Initial Term Facility raised by the Issuer on the Initial Issue Date.

The Issuer advanced the proceeds of the Second Artesian Term Facility to SWS under an Issuer/SWS Loan Agreement dated 5 July 2004 (the "**Second Issuer/SWS Loan Agreement**"). The advance under the Second Issuer/SWS Loan Agreement is equal to the principal amount of the Second Artesian Term Facility.

The Issuer advanced to SWS the proceeds of each Sub-Class of Series 2 Bonds under an Issuer/SWS Loan Agreement dated 27 May 2005 (the "**Third Issuer/SWS Loan Agreement**"). Each advance under the Third Issuer/SWS Loan Agreement is equal to the principal amount of the corresponding Sub-Class of Series 2 Bonds.

The proceeds of all Financial Indebtedness raised by the Issuer through the further issue of Bonds or raising of debt under any Authorised Credit Facility (other than the DSR Liquidity Facilities) will be lent to SWS under further Issuer/SWS Loan Agreements in order that such Financial Indebtedness will be backed by a debt obligation owed to the Issuer under such Issuer/SWS Loan Agreement. Such debt will be subdivided into advances such that each advance corresponds to the principal amounts of the relevant Tranche, Sub-Class or Class of Bonds issued or the principal amount of debt raised under the relevant Authorised Credit Facility or Facilities by the Issuer.

All advances made or to be made by the Issuer under the Issuer/SWS Loan Agreements are or will be in Sterling and in amounts and at rates of interest set out in the relevant Final Terms or Authorised Credit Facility or, if hedged in accordance with the Hedging Policy (see "*Hedging Agreements*" below), at the hedged rate plus, in each case, a small margin and will have interest payment dates on the same dates as the related Bonds or advance under the relevant Authorised Credit Facility. Interest on each advance made under an Issuer/SWS Loan Agreement will accrue from the date of such advance. In addition, each advance will be repayable on the same date as the related Bonds or advance under the relevant Authorised Credit Facility.

The obligations of SWS under each Issuer/SWS Loan Agreement are or will be secured pursuant to the Security Agreement, and such obligations are or will be guaranteed by SWSH and SWSGH in favour of the Security Trustee, who holds or will hold the benefit of such security on trust for the Secured Creditors (including the Issuer) on the terms of the STID.

The Issuer's obligations to repay principal and pay interest on the Bonds are intended to be met primarily from the payments of principal and interest received from SWS under each Issuer/SWS Loan Agreement.

SWS agrees to make payments free and clear of any withholding on account of tax unless it is required by law to do so — in such circumstances SWS will gross-up such payments.

In the Common Terms Agreement, SWS makes certain representations and warranties (as more fully set out under "*Common Terms Agreement — Representations*" below) to each Finance Party (which includes the Issuer as lender under an Authorised Credit Facility).

Each Issuer/SWS Loan Agreement is or will be governed by English law and subject to the exclusive jurisdiction of the English courts (except that the Issuer alone may commence proceedings in any other court with jurisdiction).

Fees Generally

The Issuer is responsible for paying the fees and expenses of the Bond Trustee, the Security Trustee, the Paying Agents, the Registrar, the Transfer Agents, the Agent Bank, the Issuer's legal advisers, accountants and auditors, certain fees due to MBIA Assurance S.A. in respect of the Financial Guarantees in relation to the Class A Wrapped Bonds issued on the Initial Issue Date and on 27 May 2005 and certain fees due to other Financial Guarantors of Wrapped Debt and to liquidity providers.

SWS, by way of facility fees under the Issuer/SWS Loan Agreements, pays to the Issuer amounts equal to the amounts required by the Issuer to pay its ongoing fees and expenses.

Common Terms Agreement

General

Each of the Existing Hedge Counterparties, the Security Trustee, the Cash Manager, the Standstill Cash Manager, the Liquidity Facility Providers, the Initial RCF Providers, the Initial Term Facility Provider, each Obligor, the Initial Mezzanine Facility Providers, the Bond Trustee, the Initial Financial Guarantor, the Principal Paying Agent, the Transfer Agent, the Registrar and others entered into a common terms agreement dated 23 July 2003 (the "**Common Terms Agreement**" or "**CTA**"). The Common Terms Agreement sets out the representations, covenants (positive, negative and financial), Trigger Events and Events of Default which apply to each Authorised Credit Facility (including for the avoidance of doubt the Issuer/SWS Loan Agreements, Hedging Agreements and any other document entered into in connection with an Authorised Credit Facility).

It is a term of the Common Terms Agreement that any representations, covenants (to the extent of being able to declare an Event of Default), Trigger Events and Events of Default contained in any document which is in addition to those in the Common Terms Agreement and any other Common Agreement and any other exception expressly set out in the CTA will be unenforceable (save for limited exceptions which, among other things, include covenants relating to indemnities, covenants to pay, covenants relating to remuneration, costs and expenses, representations and covenants in each Class or Sub-Class of Bonds and certain provisions under the Hedging Agreements and the Finance Leases). The Common Terms Agreement allows SWS (following a Periodic Review or any material change in the regulation of the water industry in the United Kingdom) to amend any financial ratio contained within the covenants, Trigger Events or Events of Default, provided that each Financial Guarantor and the Security Trustee (acting on the instructions of the Majority Creditors) agree and the relevant ratings set out in the definition of Rating Requirement (in relation to the Class A Bonds) and the ratings ascribed to the Class B Bonds at the time of their issue have been affirmed by all Rating Agencies then rating the Class A Bonds and/or Class B Bonds as applicable.

The Common Terms Agreement also sets out the cash management arrangements to apply to the SWS Financing Group (see "*Cash Management*" below). It is a requirement of the Common Terms Agreement that future providers of Authorised Credit Facilities must also accede to the Common Terms Agreement and the STID.

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

Representations

On the Initial Issue Date each Obligor made a number of representations in respect of itself to each Finance Party. These representations include (subject, in some cases, to agreed exceptions and qualifications as to materiality and reservations of law) representations as to:

(i) its corporate status, power and authority (a) to enter into and perform its obligations under the Transaction Documents and (b) to own, lease and operate its assets and to carry on its business;

(ii) its obligations under the Transaction Documents being its legal, valid and enforceable obligations;

(iii) its entry into and performance under the Transaction Documents not conflicting with any document which is binding upon its assets (or, in the case of SWS, its material assets), its constitutional documents or any material applicable law (save in the case of SWS and the Instrument of Appointment to the extent such conflict has been waived by Ofwat to the reasonable satisfaction of the Security Trustee);

(iv) the preparation of its financial statements in accordance with Applicable Accounting Principles and that such financial statements give a true and fair view of its financial condition;

(v) no event having occurred or circumstance having arisen since the date of the last financial statements which has a Material Adverse Effect (except for any announcement of K from time to time);

(vi) except as disclosed in its financial statements, it not being subject to any contingent liabilities or commitments that would be reasonably likely to have a Material Adverse Effect;

(vii) the validity and admissibility in evidence of the Finance Documents in any proceedings in the jurisdiction of its incorporation;

(viii) the Security Documents to which it is party conferring the Security Interests they purport to confer and such Security Interests not being subject to any prior or *pari passu* Security Interest (other than a Permitted Security Interest);

(ix) the conduct of its business not violating any judgment, law or regulation, which if enforced would have a Material Adverse Effect;

(x) no Default or Potential Trigger Event being outstanding or will result from entry into and performance under the Transaction Documents;

(xi) the obtaining by it prior to the Initial Issue Date of all consents and approvals necessary for the conduct of SWS' business and the transactions in the Finance Documents which if not obtained or complied with, or which if revoked or terminated, would either (i) have a Material Adverse Effect or (ii) not be in the normal course of business and Good Industry Practice generally;

(xii) its ownership of, or interests in, the assets over which it has created Security Interests under the Security Documents and which are material to the operation of its business;

(xiii) insurances required to be maintained under any Finance Document being in full force and effect where failure to maintain would be reasonably likely to have a Material Adverse Effect;

(xiv) there being no insolvency event in relation to it;

(xv) the ownership structure of the SWS Financing Group;

(xvi) the due payment of all its taxes (save to the extent any tax payment is being disputed in good faith) and the due filing in all material respects of any tax returns and there being no material claims being asserted against it with respect to taxes which are not being disputed in good faith);

(xvii) under the laws of its jurisdiction of incorporation and tax residence in force on the Initial Issue Date, it not (other than as disclosed) being required to make any deduction or withholding from any payment of interest under the Finance Documents in circumstances where, under current United Kingdom law, no United Kingdom withholding tax would be imposed on the payment;

(xviii) the claims of Secured Creditors secured pursuant to a Security Agreement ranking prior to the claims of its other unsecured and unsubordinated creditors;

(xix) no Security Interest having been created, or allowed to exist, other than Permitted Security Interests and no indebtedness incurred other than Permitted Financial Indebtedness and Permitted Volume Trading Arrangements;

(xx) the Bonds constituting (or constituting upon execution, due authentication and delivery) legal and valid obligations binding on the Issuer and enforceable against it in accordance with its terms and constituting evidence of direct, secured and unconditional obligations of the Issuer;

(xxi) no litigation or other proceedings current, or to its knowledge pending or threatened against it or its assets which, if adversely determined, are reasonably likely to have a Material Adverse Effect;

(xxii) limits on its powers not being exceeded as a result of the borrowing, leasing, granting of security or giving or guarantees contemplated by the Finance Documents;

(xxiii) compliance with environmental laws and having obtained all environmental permits necessary for conduct of its business and no environmental claim having been commenced;

(xxiv) no loans made by any Obligor being outstanding to other persons immediately following the issue of Bonds on the Initial Issue Date other than pursuant to Finance Documents, under any Permitted Volume Trading Arrangements and the SWS/SWSG Loan Agreement;

(xxv) no Treasury Transactions being outstanding immediately following the issue of Bonds on the Initial Issue Date other than the Initial Hedging Agreements;

(xxvi) all arrangements or contracts with any person being on arm's length basis and, other than in respect of contracts entered into by SWS and under which payments to be made would fall within paragraph (a) of the exclusions in the definition of Distribution, on terms no less favourable to it than would reasonably be expected to be obtained in a comparable arm's length transaction with a person not being an Associate, except: (1) contracts entered into by SWS and under which payments to be made would fall within paragraph (c) of the exclusion in the definition of Distribution; (2) as permitted under the Finance Documents; or (3) as a result of a Permitted Emergency Action; and

(xxvii) on the Initial Issue Date, no member of the SWS Financing Group being liable in any manner in respect of any Financial Indebtedness (including by way of primary obligor, guarantor, surety or any other manner) that is not Class A Debt, Class B Debt or Mezzanine Debt, the providers of which have executed the CTA and the STID, the SWS Preference Shares, the initial holders of which will have executed the SWS Preference Share Deed, or Permitted Financial Indebtedness falling within the categories listed in paragraphs (a), (b), (d) or (e) of the definition of Permitted Financial Indebtedness.

Also, on each Issue Date and on each date on which any Financial Guarantee or any other new Authorised Credit Facility is issued or entered into under the Programme, each Obligor will repeat certain of such representations (excluding those representations contained in paragraphs (x), (xxv) and (xxvii) above on each Issue Date and excluding the representation contained in paragraph (xx) on each date on which any Financial Guarantee or any other new Authorised Credit Facility is issued or entered into under the Programme) in relation only to the Bonds or Financial Guarantee then being issued or the new Authorised Credit Facility then being entered into (the "Initial Date Representations").

On each Payment Date, on each date of a request for a borrowing, on the first date of each borrowing and on each date for payment of a Restricted Payment, each Obligor shall make certain representations (including those contained in paragraphs (i), (ii), (iv), (v), (vi), (xiii), (ix), (xxi), (xxii) and (xxiii) above) (the "Repeated Representations"). Each Obligor shall also make the Repeated Representations on each date on which SWS enters into any new Material Agreement, but only in relation to such new Material Agreement.

Additionally, SWS has made and will make (subject, in some cases, to agreed exceptions and qualifications as to materiality and reservations of law) representations including:

(i) (on the date of each Initial Date Representation and each Repeated Representation) to the best of its knowledge, it has the right to use Intellectual Property Rights necessary to conduct its Business;

(ii) (on the date of each Initial Date Representation) to the best of its knowledge (and save as disclosed to the Security Trustee) all parties to Transaction Documents are in compliance with the Transaction Documents;

(iii) (on the date of each Initial Date Representation) assumptions used in respect of financial ratio calculations and projections having been made in good faith, after due and careful consideration and being consistent with Applicable Accounting Principles and Good Industry Practice;

(iv) (on the date of each Initial Date Representation and each Repeated Representation) it is not aware of any Special Administration Order having been made in respect of it; and

(v) (on the date of each Initial Date Representation) the accuracy (in all material respects) of certain written information provided by SWS and the accuracy of this Prospectus.

Additionally, each of SWSH, SWSGH and the Issuer represents that its activities have been limited to the First Aqua Acquisition, the financing and refinancing thereof following the acquisition by SWI of the Issuer in May 2003 the holding of shares in its subsidiaries, implementing the corporate reorganisation of SWI and its subsidiaries on the Initial Issue Date, the declaration and payments of dividends, and its entry into and performance of documents relating thereto and envisaged by the Transaction Documents.

Covenants

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

Information — Covenants

(i) So far as permitted by any applicable law or any binding confidentiality obligation, SWS has undertaken to supply to the Security Trustee, each Rating Agency rating the Bonds at that time and, in certain cases, each Financial Guarantor certain information such as:

a) a copy of all information, which would reasonably be expected to be material to an Authorised Credit Provider to the SWS Financing Group, which it supplies to the Director General;

b) as soon as reasonably practicable after becoming aware, details of any proposed material changes to the Instrument of Appointment or any proposed changes to the constitutional documents of any member of the SWS Financing Group;

c) promptly upon becoming aware, details of any actual or potential enquiry, investigation or proceeding commenced by any government, court, regulatory agency or authority, if such enquiry, investigation or proceeding would be reasonably likely to have a Material Adverse Effect;

d) as soon as reasonably practicable after receipt, any material notice (including an enforcement notice) from any governmental authority or industry regulator (including Ofwat) received by SWS;

e) copies of all certificates and responses provided by SWS or any member of the SWS Financing Group to any industry regulator (including Ofwat) which would reasonably be expected to be material and adverse and which relates to the creditworthiness of SWS or SWS' ability to perform its duties under the Instrument of Appointment;

f) copies of all reports and information provided by the operator and/or service provider to it under any Material Agreement which would be materially adverse in relation to the creditworthiness of SWS or to SWS' ability to perform its duties under the Instrument of Appointment;

g) a semi-annual Investors Report; and

h) such material information about the business and financial condition of SWS as a Secured Creditor may reasonably and properly request, from time to time, on the request of the Security Trustee (as directed by such Secured Creditor).

(ii) SWS has further agreed to provide information regarding certain changes of control of SWSGH to the Security Trustee, each Financial Guarantor, and the Rating Agencies as soon as it becomes aware of any such proposal and to use all reasonable endeavours to procure that the Security Trustee and each Financial Guarantor have been given a reasonable opportunity to express views on the identity and role of any such proposed new Controlling person under any such changes of control.

(iii) SWS has further agreed to provide information in relation to any announcement of K which has or might reasonably have a Material Adverse Effect.

(iv) SWS has further agreed to use all reasonable endeavours to supply any information due to, or requested by, the Director General within the time period provided for supply of such information. If no time period is specified, SWS must provide the required information as soon as reasonably practicable. This is subject to action SWS reasonably believes is consistent with prudent management as part of negotiations with the Director General.

(v) Additionally, each Obligor has undertaken to supply to the Security Trustee within a certain timeframe:

a) its audited financial statements for each of its financial years and, in the case of SWS, its unaudited financial interim statements, for the first half-year of each of its financial years;

b) copies of all material documents despatched by it to its shareholders (to the extent that such documents would be sent to its shareholders if such Obligor were a listed company) or creditors generally;

c) as soon as reasonably practicable after becoming aware or available, details of:

(A) any litigation or other proceedings (which alone or in aggregate could reasonably be expected to give rise to a claim against SWS of £5,000,000 (indexed)), which are current, threatened or pending and would be reasonably likely, if adversely determined, to have a Material Adverse Effect;

(B) the periodic information relating to it (such as SWS' annual charges scheme, a summary of SWS' strategic business plan at each Periodic Review, SWS' current Procurement Plan (if any), SWS' annual drinking water quality report, SWS' annual environmental report and SWS' annual conservation and access report);

(C) promptly upon coming aware of them, details concerning any Obligor placed on credit watch with negative implications;

(D) any event which could reasonably be expected to give rise to an insurance claim in excess of £4,000,000 (indexed from the Initial Issue Date);

(E) any Material Entity Event (see "*Material Entity Events*" below) and/or Emergency which would be reasonably likely to have a Material Adverse Effect;

(F) any non-compliance with any law or regulation which would be reasonably likely to have a Material Adverse Effect;

(G) any other event which would be reasonably likely to have a Material Adverse Effect;

d) such material information as is reasonably and properly requested by any Secured Creditor; and

e) notification of any Default or Potential Trigger Event relating to it promptly upon becoming aware of its occurrence (and the steps, if any, being taken to remedy it).

(vi) Additionally, each of SWS and the Issuer has undertaken, among other things:

a) to supply a compliance certificate signed by two authorised signatories of the Issuer and two directors of SWS; such compliance certificate to be accompanied by a statement as to what the historical and forward-looking financial ratios which are required to be calculated under the Common Terms Agreement are and a copy of the computations made in respect of such historical and forward-looking financial ratios;

b) to permit the Security Trustee to investigate the calculations contained in any compliance certificate and to call for other substantiating evidence if it certifies to SWS or the Issuer that it has reason to believe that the historical or forward-looking ratios (or confirmation of compliance with the financial ratios) as set out in the statement are incorrect or misleading or in the event that there is a deterioration in the historical ratios; and

c) to deliver to the Security Trustee promptly after any reasonable request made by the Security Trustee, a certificate signed on its behalf by two of its authorised signatories (a) certifying that no Default or Potential Trigger Event is outstanding of which it is aware, having made all reasonable enquiries, or if a Default or Potential Trigger Event is outstanding, specifying the Default or Potential Trigger Event and the steps (if any) taken or proposed to be taken to remedy such event.

(vii) In addition, each Obligor in respect of information delivered electronically:

a) may deliver any information under the Common Terms Agreement to a Secured Creditor by posting it on an electronic website, provided the Obligor and the Security Trustee have designated a website and the Obligor has notified the Security Trustee and each relevant Secured Creditor of the address and password for such website; and

b) must notify the Security Trustee if (i) the website cannot be accessed or the website or any information on it is infected for a period of five consecutive days, in which case the Obligor must supply the Security Trustee with all information required under the Common Terms Agreement in paper form with copies as requested by any Finance Party or (ii) if the password is changed.

Covenants — General

(i) Each Obligor has undertaken, among other things:

a) to do all such things as are necessary to maintain its corporate status where failure to do so would be reasonably likely to have a Material Adverse Effect or otherwise adversely affect the Security Interests of the Secured Creditors;

b) to comply with its cash management obligations (if any) set out in the Common Terms Agreement;

c) to ensure that the secured claims of Secured Creditors against it under the Finance Documents will rank (subject to certain reservations as to matters of law) prior to the claims of all its other unsecured and unsubordinated creditors save for those whose claims are preferred solely by law;

d) to operate and maintain, or ensure the operation and maintenance of, its business in a safe, efficient and business-like manner and in accordance with its memorandum and articles of association or other constitutional documents and the Finance Documents and, in the case of SWS, the Instrument of Appointment, the WIA and Good Industry Practice (taking its Business as a whole);

e) to comply with the terms of the Transaction Documents to which it is a party;

f) to maintain and take all reasonable steps to enforce its rights and exercise its discretions under the Transaction Documents in accordance with Good Industry Practice;

g) to ensure that, save as otherwise agreed by the Security Trustee and each Financial Guarantor and save for any Permitted Acquisitions or Permitted Disposals, the corporate ownership structure of the SWS Financing Group (other than the ownership or Control of SWSGH and the ownership of the SWS Preference Shares) remains as at the date of the Common Terms Agreement;

h) so far as permitted by applicable law and regulatory requirements, to execute all such further documents and do all such further things as the Security Trustee (acting reasonably) may consider necessary to give effect to the Finance Documents;

i) (A) to take all such action as the Security Trustee may reasonably require for the purpose of perfecting, protecting and preserving the rights of the Security Trustee under the Security Documents and the Security Interests under the Security

Documents; and (B) to take all actions as the Security Trustee may require, following the making of any acceleration, cancellation or demand under the Issuer/SWS Loan Agreements or the termination of, or prepayment of the rentals relative to, the leasing of the Equipment in each case after the occurrence of a Default for facilitating the exercise of the rights of the Security Trustee under the Security Documents and/or the realisation of any Security Interests under the Security Documents; and (C) to use all reasonable endeavours to receive acknowledgements of assignment from such counterparties as the Security Trustee may nominate;

j) not to incur any Financial Indebtedness other than Permitted Financial Indebtedness or, in the case of SWS, Permitted Volume Trading Arrangements;

k) not to enter into any amalgamation, demerger, merger, consolidation or reconstruction other than as agreed by the Security Trustee and each Financial Guarantor (other than, in the case of SWS, a Permitted Disposal or Permitted Acquisition);

l) not to acquire or invest, other than Permitted Acquisitions and Authorised Investments;

m) not to be a creditor in respect of any Financial Indebtedness or issue any guarantee or indemnity in respect of the obligations of any other person except for (A) any credit or indemnity provided under any Finance Document; (B) any loan made under the Issuer/SWS Loan Agreements; (C) any loan provided to SWS subordinated to the Authorised Credit Facilities on terms acceptable to the Security Trustee; (D) any guarantee in the Finance Documents; (E) the SWS/SWSG Loan; (F) single loans by SWS to employees of less than £250,000 (indexed from the Initial Issue Date) or loans by SWS to employees in aggregate less than £750,000 (indexed from the Initial Issue Date); (G) in the case of SWS, Permitted Volume Trading Arrangements; (H) any loan made as a Permitted Post Closing Event; (I) other loans by SWS in aggregate of less than £500,000 (indexed from the Initial Issue Date) not falling in (A) to (H) above; provided (other than in the case of (B) and except where a Default is continuing (F)) that no Default or Potential Trigger Event is continuing at the time any such credit or loan or guarantee is proposed to be made or issued;

n) not to change its memorandum or articles of association or other constitutional documents without the prior written consent of the Security Trustee (provided that SWS may change its memorandum or articles of association or other constitutional documents without the Security Trustee's consent where such change is not in relation to the SWS Preference Shares and would not be reasonably likely to have a Material Adverse Effect or otherwise prejudice the Security Interests created pursuant to the Security Documents);

o) not to enter into any Treasury Transaction other than Hedging Agreements;

p) except for a Permitted Tax Loss Transaction, not to enter, without the consent of the Security Trustee and each Financial Guarantor, into any arrangements with any other company or person (other than a taxation authority in respect of the taxation liabilities of such Obligor or any other Obligor or pursuant to the Finance Documents) relating to Tax;

q) not to compromise or settle any claim, litigation or arbitration without prior notification to the Security Trustee if any such compromise or settlement would be reasonably likely to have a Material Adverse Effect;

r) (A) to promptly obtain, maintain and comply with the terms of all applicable laws, regulations and orders and obtain and maintain all governmental and regulatory consents, licences, authorisations and approvals (including the Instrument of Appointment) necessary for the conduct of its business, for entry into and performance of the Finance Documents, and for the leasing of the Equipment, as a whole in accordance with Good Industry Practice and (B) to do nothing which would lead to the termination, suspension or revocation of any such consents, licences, authorisations and approvals, in each case where such failure would be reasonably likely to have a Material Adverse Effect;

s) to maintain separate bank accounts;

t) to pay all Taxes for which an Obligor is primarily liable and other outgoings prior to penalties being incurred unless payment of those Taxes is being contested in good faith by appropriate means which permit the deferral of payment and/or an adequate reserve has been set aside for payment of those Taxes;

u) not to create or allow to exist any Security Interest on the Equipment or any of its present or future revenues or assets other than Permitted Security Interests, nor create or enter into any restriction or prohibition on the creation or granting of, any Security Interest on any of its assets except as permitted by the Finance Documents, nor create or permit to exist any further Security Interest over all or any of its present and future revenues, equipment or assets as security for any Permitted Financial Indebtedness other than in favour of the Security Trustee to be held upon the terms of the STID;

v) not to (A) (i) sell, transfer or otherwise dispose of any of its assets on terms where it is or may be leased to or re-acquired or acquired by any Associate other than (in the case of the Issuer or SWS) pursuant to a Finance Lease; or (ii) sell, transfer or otherwise dispose of any of its receivables (other than Permitted Book Debt Disposals); or (iii) purchase any asset on terms providing for a retention of title by the vendor or on conditional sale terms or on terms having a like substantive effect to any of the foregoing except for assets acquired in the ordinary course of its business carried on in the normal course, in each case (in respect of SWS only), in circumstances where the transaction is entered into primarily as a method of raising Financial Indebtedness or of Financing the acquisition of an asset, nor (B) enter into any such transaction in (A) above in circumstances where

the transaction is not entered into primarily as a method of raising finance to the extent that the consideration in respect of such sales, leases, transfers or disposals is not received in cash payable in full at the time and exceeds an amount equal to 0.13 per cent. of RCV in aggregate at any time;

w) not to dispose of all or any part of the Equipment or its undertaking, revenues, business or assets other than a Permitted Disposal or pursuant to the creation of a Permitted Security Interest;

x) not to change its tax residence from the United Kingdom;

y) not to (A) redeem, repurchase, defease, retire or repay any of its share capital or resolve to do so; (B) issue any shares which by their terms are redeemable or convertible or exchangeable for Financial Indebtedness; or (C) after the Initial Issue Date, issue any share capital to any person, other than where any such action or transaction: (i) is in respect of the SWS Preference Shares (subject, in certain circumstances, to the Restricted Payment Condition); (ii) is in furtherance of a Restricted Payment and the amount of the Restricted Payment is permitted to be paid pursuant to the Finance Documents; (iii) is expressly permitted under the Finance Documents; or (iv) has received the prior written consent of the Security Trustee and each Financial Guarantor;

z) other than as a result of Permitted Emergency Action (in which case SWS shall use reasonable endeavours to ensure that all contracts entered into will be on an arm's length basis, although SWS will not be required to obtain alternative competitive quotes) or in respect of contracts entered into by SWS under paragraph (c) of the definition of Distributions, not to enter into any arrangement or contract with any person otherwise than on an arm's length basis save as has been disclosed or unless expressly permitted under the Finance Documents; and

aa) other than SWS except with the consent of the Security Trustee and each Financial Guarantor, no Obligor shall participate in a scheme in respect of retirement benefit arrangements with companies other than the other Obligors. SWS may participate in subject to paragraphs (iv) and (v) below, the Permitted Existing Pension Schemes.

(ii) Additionally, each of SWSH and SWSGH has undertaken:

a) not to: (A) carry on or transact any business or other activity other than (i) ownership of the shares in members of the SWS Financing Group held by it on the Initial Issue Date; (ii) the giving of guarantees in accordance with the Finance Documents; and (iii) performance of obligations required under the Finance Documents; (B) own any asset or incur any liabilities except for the purposes of carrying on that business in accordance with the Finance Documents; (C) suspend, abandon or cease to carry on its business; (D) declare, make or pay Restricted Payments otherwise than as permitted under the Finance Documents;

or (E) take any steps to enforce any claims it may have against any other Obligor without the prior written consent of the Security Trustee; and

b) not to make any Restricted Payments otherwise than out of monies received by it, directly or indirectly, from SWS which have been properly paid by SWS as a Distribution or as set out under the Common Terms Agreement.

(iii) Save as otherwise approved by the Security Trustee, SWS has further undertaken to maintain on its board of directors at least three non-executive directors who are not employees or directors of any Associate (subject to temporary vacancies arising out of exceptional circumstances).

(iv) Additionally, SWS has undertaken among other things:

a) to ensure that the nature of its business is limited to the Business;

b) to conduct its Appointed Business in the name of SWS only and to ensure that separation from the Group or Associates is maintained at all times by holding SWS out as a separate entity, correcting any misunderstanding as to identity and using stationery, invoices and cheques separate from any other person or entity;

c) not to permit, agree to or recommend any suspension or the abandonment of all or a material part of the operation of its Appointed Business unless such suspension or abandonment is in accordance with its Instrument of Appointment;

d) if it exceeds the Permitted Non-Appointed Business Limits, to dispose of or reduce all or part of its Permitted Non-Appointed Business within six months so that the Permitted Non-Appointed Business Limits are complied with on the next Calculation Date;

e) to comply in all material respects with the Instrument of Appointment save to the extent Ofwat has waived or approved such non-compliance to the reasonable satisfaction of the Security Trustee;

f) not to agree to any amendment or variation of the Instrument of Appointment which would reasonably be expected to have a Material Adverse Effect;

g) to comply with applicable relevant Environmental Laws and Environmental Approvals applicable to it, where failure to do so would be reasonably likely to have a Material Adverse Effect;

h) as soon as reasonably practicable upon becoming aware of the same, notify the Security Trustee of: (A) any environmental claim that is current or, to the best of its knowledge and belief, is threatened; or (B) any facts or circumstances which will or are reasonably likely to result in an environmental claim being commenced or threatened against it, which, in either case if substantiated, is reasonably likely either to have a Material Adverse Effect or result in any material liability for a Finance Party;

i) to effect and maintain those insurances in connection with its Business as are required under the Common Terms Agreement;

j) to take all reasonable action to safeguard and maintain such present and future rights in accordance with Intellectual Property Rights necessary for its Business including observing all covenants and stipulations relating thereto and obtaining all necessary registrations;

k) (A) other than in respect of contracts entered into by SWS and under which payments to be made would fall within paragraphs (a) or (c) of the exclusions in the definition of Distribution, to comply with the Outsourcing Policy, which became effective on and from the Initial Issue Date and applies to each Outsourcing Agreement and Capex Contract entered into by SWS (other than any Excluded Agreements) on and from the Initial Issue Date; (B) subject to (A), to procure that any Outsourcing Agreement or Capex Contract entered into on and from the Initial Issue Date complies with the Public Procurement Rules (if such Outsourcing Agreement or Capex Contract would be an agreement to which the Public Procurement Rules would apply) and the Outsourcing Policy; (C) where an Emergency is continuing, to use its best endeavours to rectify such Emergency as soon as is reasonably practicable (for the avoidance of doubt, any Permitted Emergency Action will not constitute a breach of the Outsourcing Policy); (D) each time an Excluded Agreement expires in accordance with its terms or is terminated early, any agreement entered into by SWS in place of such Excluded Agreement shall comply with the Outsourcing Policy (to the extent required by the terms of the Outsourcing Policy); (E) not to amend, modify or alter any material provision or agree to renew or extend (or agree to exercise any option to renew or extend) any Excluded Agreement without the consent of the Security Trustee and each Financial Guarantor; and (F) to at all times use Good Industry Practice in exercising its rights and performing its obligations under any Excluded Agreement. In March 2005 SWS obtained a waiver from the Majority Creditors in relation to certain aspects of the Single Entity Contract described in Chapter 4 (*Description of the SWS Financing Group – Capital Investment Programme*) that do not comply with the Outsourcing Policy – see "*Events of Default*" below;

l) to ensure it has adequate financial and management resources to enable it to discharge its core obligations under the Instrument of Appointment and under the Transaction Documents and, in respect of performance obligations which are either passed on to a Contractor or outsourced, it has retained sufficient control to discharge its obligations under the Instrument of Appointment and under the Transaction Documents;

m) following receipt of notice of termination of the Instrument of Appointment, SWS must use its reasonable endeavours to ensure that subject to its obligations under the WIA: (A) a Transfer Scheme is agreed between SWS, the transferee and the Director General by a date no less than two years prior to the expiration of such notice; and (B) any such Transfer Scheme will not be prejudicial to the interests of the Secured Creditors;

n) to use all reasonable endeavours to ensure that the Security Trustee is joined in the consultation process with the Director General if SWS becomes subject to any Transfer Scheme;

o) subject to its obligations under the WIA, not to agree to any Transfer Scheme without the consent of the Security Trustee and each Financial Guarantor;

p) other than in respect of the SWS Preference Shares, to ensure that there are no agreements in force or corporate resolutions passed which call for the present or further issue or allotment of, or grant to any person other than SWSH, the right (whether conditional or otherwise) to call for the issue or allotment of any share (or equivalent) loan note or loan capital of SWS (including an option or right of pre-emption or conversion);

q) to make an SWS/SWSG Debt Service Distribution quarterly each year and then only provided that certain conditions are met, including each of the following:

   (i) no Event of Default is subsisting or will result from the payment;

   (ii) no event of default has occurred and is continuing under the SWS/SWSG Loan Agreement and SWSG is not in default of its obligations under the SW Tax Deed of Covenant;

   (iii) all dividends declared by SWS, SWSH and SWSGH are validly declared;

   (iv) all payments in respect of a Permitted Tax Loss Transaction comply fully with the SW Tax Deed of Covenant and the CTA; and

   (v) such SWS/SWSG Debt Service Distribution is made against irrevocable payment instructions directing the Account Bank to remit the proceeds thereof on receipt by SWSG to the relevant account of SWS for same day value;

r) to comply with the obligations to provide information under any Surveillance Letter or any Authorised Credit Facility;

s) to apply to the Director General for an IDOK when permitted under the Instrument of Appointment (or use any other means available to apply for an IDOK), in all circumstances which are appropriate in accordance with Good Industry Practice provided that any such application is consistent with prudent management;

t) to levy charges to customers which, together with other available amounts, are as far as possible sufficient, within the constraints of the current price control framework, to enable SWS to meet its operational, investment and financial obligations on a timely basis under the Instrument of Appointment and its obligations in respect of Financial Indebtedness;

u) not to propose any resolution for, or agree to any material amendments to, variation, modification, waiver, suspension, revocation, termination of any Material Agreement save in accordance with the Outsourcing Policy without the prior written consent of the Security Trustee; and

v) to (i) procure that the nature of the business of its Pension Companies is limited to the business and functions of a trustee of an occupational pension scheme (as defined in section 1 of the Pension Schemes Act 1993) in respect of SWS Pension Schemes only and (ii) procure that the Pension Companies do not incur any Financial Indebtedness or permit security to be taken over their assets or shares other than where such Security is taken in accordance with the Security Agreement.

(v) Additionally, SWS and the Issuer have undertaken among other things:

a) to maintain a rating of the Class A Debt and Class B Debt and a shadow rating of Class A Wrapped Debt with any two of the Rating Agencies;

b) only to:

(A) pay Customer Rebates at a time when no Event of Default is subsisting;

(B) other than in the case of Permitted Post Closing Events, any SWS/SWSG Debt Service Distribution, any Subordinated Debt Replacement Event and any SWS Preference Share Conversion Event, pay any Distribution or make any payment under the Subordinated Debt or SWS Preference Shares if:

(i) in the case of Distributions or dividends under the SWS Preference Shares the payment is made after a duly constituted board meeting has been held approving the declaration of such Distribution or dividend;

(ii) the amount of the Distribution, payment under the Subordinated Debt and/or payment under the SWS Preference Shares that may be paid is limited to an amount equal to the Proposed Payment Amount (as defined below);

(iii) on the date of such payment:

a) no drawings are outstanding under the Liquidity Facilities, other than Standby Drawings; and

b) save in the case of the first scheduled payment under the Subordinated Debt and the SWS Preference Shares, the Senior RAR, as certified by the Issuer and SWS in the Compliance Certificate most recently delivered to the Security Trustee and each Rating Agency, is less than or

equal to. 0.850:1 for each Test Period (after deducting an amount equal to the aggregate of any proposed Customer Rebates, proposed Distribution, proposed payment on the Subordinated Debt and proposed payment on the SWS Preference Shares (the "**Proposed Payment Amount**") from available cash); and

c) no Default subsists or might reasonably be expected to result from the payment and the Repeated Representations are, and will following such payment remain, correct, provided that if such Default arises as a result of a notice to terminate the Instrument of Appointment having been served then such Default shall be deemed to be cured if an independent financial adviser shall have certified to the Security Trustee that a Transfer Scheme as defined in Schedule 2 of the WIA or other satisfactory security has been established that will not be materially prejudicial to the interests of Class A Debt Providers or the Class B Debt Providers (as the case may be); and

(iv) in the case of a payment under the SWS Preference Shares or any Subordinated Debt into which the SWS Preference Shares have converted, at the time of such payment there is no amount which has fallen due under the Subordinated Debt which has not been paid or would, but for any deferral of unpaid amounts, have fallen due,

and SWS shall be treated as having made to each Secured Creditor in respect of Class A Debt and Class B Debt a representation on the date of any Restricted Payment that each of the conditions necessary to be satisfied in relation to such Restricted Payment has been satisfied.

In addition to the restrictions on payment of Restricted Payments described above, a Restricted Payment will not be permitted if certain changes of control of SWSGH result in a downgrade of the shadow rating of the Class A Wrapped Debt to or below BBB+ (S&P), Baa1 (Moody's) and BBB+ (Fitch) and such ratings have not been restored;

(c) to agree to co-operate with the Rating Agencies in connection with any reasonable request for information in respect of the maintenance of a shadow rating or rating and with any review of its business which may be undertaken by one or more of the Rating Agencies after the date of the Common Terms Agreement;

(d) to ensure that there are installed and maintained accounting, management information, financial modelling and cost control systems which are of such a standard which can produce the information required within the time set out in the Finance Documents and procure that there are maintained books of account and

other records adequate to reflect fairly and accurately its financial condition, the results of its operations and to provide the reports required to be delivered pursuant to the Finance Documents;

(e) to authorise the Auditors to communicate directly with the Security Trustee at such time as such parties may reasonably require (and whilst any Default is outstanding at any time) regarding its accounts and operations and furnish to the Security Trustee a copy of such authorisation, subject to the Auditors' agreement to communicate at such time and upon agreed conditions;

(f) to inform the Security Trustee of any change to the Auditors, as soon as reasonably practicable;

(g) to only replace the Auditors without the prior written approval of the Security Trustee if the replacement Auditors are a firm of independent public accountants of international standing;

(h) not to change its financial year end without the prior written consent of the Security Trustee, such consent not to be refused if Ofwat requires the relevant financial year to be changed, in which case SWS will change the financial covenant calculations in such manner as the Security Trustee deems necessary to enable such calculations to continue to be calculated from the relevant financial statements of SWS; and

(i) to ensure that it will not enter into any Authorised Credit Facility (other than in respect of any Subordinated Debt) unless following such entry into of such Authorised Credit Facility: (a) its aggregate nominal outstanding Financial Indebtedness which has an expected maturity falling within any period of 24 consecutive months shall not exceed 20 per cent. of SWS' RCV for the time being, and (b) the aggregate nominal outstanding Financial Indebtedness which has an expected maturity falling within the period from one Periodic Review to the next Periodic Review shall not exceed 40 per cent. of SWS' RCV for the time being (adjusted and increased proportionately to the extent that the period from one Periodic Review to the next Periodic Review is greater than five years).

(vi) Additionally, the Issuer has undertaken, among other things:

a) not to (A) carry on any business other than the raising of funds to provide debt financing to SWS for the purposes of its Business in accordance with the Finance Documents or any Hedging Agreement in accordance with the Hedging Policy; (B) own any assets or incur any liabilities except as required or permitted pursuant to the Finance Documents; (C) suspend, abandon or cease to carry on its business; or (D) take any steps to enforce any claims it may have against any other Obligor without the prior written consent of the Security Trustee;

b) to enter into the hedging arrangements contemplated in the Hedging Policy, in accordance with the terms of the Hedging Policy;

c) prior to any refinancing of any Class B Debt with any Class A Debt, to obtain confirmation from all Rating Agencies then rating the Bonds that the Rating Requirement is met and will not cease to be met as a result of such refinancing;

d) to use all reasonable endeavours to procure the admission of all listed Bonds for trading on the Market or the PSM, or such other stock exchange approved by the Dealers and the Bond Trustee, and to maintain such admission until none of the relevant listed Bonds is outstanding;

e) upon receiving a written request from the Bond Trustee, to deliver to the Bond Trustee a certificate of the Issuer setting out *inter alia* details of the aggregate principal amount outstanding under the outstanding Bonds purchased by the Issuer and as are held by any person for the benefit of any member of the SWS Financing Group, any Financial Guarantor or, so far as the Issuer is aware, any of their respective Affiliates, holding companies and subsidiaries;

f) to send or procure to be sent (not less than three days prior to the date of publication) to the Bond Trustee for the Bond Trustee's approval, one copy of each notice to be given to the Bondholders in accordance with the Conditions and not to publish such notice without such approval and, upon publication, send to the Bond Trustee two copies of such notice (such approval, unless so expressed, not to constitute approval for the purpose of Section 21 of the FSMA of such notice as an investment advertisement (as therein defined));

g) to procure that the Principal Paying Agent notifies the Bond Trustee forthwith if it does not, on or before the due date for payment in respect of the Bonds, receive unconditionally the full amount in the correct currency of the monies payable on such due date;

h) to forthwith give notice to the Bondholders of payments made after their due date to the Principal Paying Agent or the Bond Trustee;

i) not less than the number of days specified in the relevant Conditions prior to the redemption or repayment date in respect of any Bond, to give to the Bond Trustee notice in writing of the amount of such redemption or repayment pursuant to the Conditions;

j) prior to giving notice to the Bondholders that it intends to redeem the Bonds pursuant to Condition 8(c) (*Redemption for Index Event, Taxation or Other Reasons*) or 8(b) (*Optional Redemption*), to provide such information to the Bond Trustee and the Financial Guarantors as the Bond Trustee and the Financial Guarantors require in order to satisfy themselves of the matters referred to in those Conditions;

k) to promptly give notice to the Bond Trustee and to the Security Trustee (A) if it is required by law to effect a deduction or withholding of Tax in respect of any payment due in respect of any Bonds listed on a recognised stock exchange (within the meaning of Section 841 of the Income and Corporation Taxes Act

1988); or (B) if a Hedge Counterparty is required to make a deduction or withholding of Tax in respect of any payment due under the relevant Hedging Agreement; or (C) if it would not be entitled to relief for Tax purposes, in any jurisdiction in which it carries on business or is resident for tax purposes, for any material amount which it is obliged to pay under the Finance Documents and which is or has been assumed in the SWS Business Financial Model to be available for relief for Tax purposes, and in each case, take such action as may be required by the Bond Trustee and Security Trustee in respect thereof;

l) while any of the Bonds remain outstanding, to give notice, or procure that notice is given, to each of the Rating Agencies of (A) any proposed amendment to the Finance Documents other than amendments that the Bond Trustee considers to be of a formal, minor or technical nature or made to correct a manifest error or necessary or desirable for clarification; (B) any request for consent from the Security Trustee and each Financial Guarantor under any Finance Document (other than the STID) in relation to any matter or act which would be automatically treated as permitted by such Finance Document upon the giving of consent by the Security Trustee and each Financial Guarantor; (C) the Bonds of any Sub-Class being repaid in full; (D) the termination of the appointment of the Cash Manager; (E) the appointment of a replacement Bond Trustee or Security Trustee or the appointment of any new or replacement Agents; (F) any Default; (G) the taking of Enforcement Action; (H) the occurrence of any SWS Change of Control or certain changes of control of SWSGH; or (I) the acquisition of any Permitted Subsidiary pursuant to a Permitted Acquisition, in each case, promptly after the Issuer or SWS becoming aware of the same;

m) to observe and comply with its obligations, and use all reasonable endeavours to procure that the Agents observe and comply with all their obligations under the Agency Agreement and, if any Registered Bonds are outstanding, to procure that the Registrar maintains the Register and to notify the Bond Trustee immediately if it becomes aware of any material breach or failure by an Agent in relation to the Bonds;

n) to give not less than 14 days' prior notice to the Bondholders of any future appointment or any resignation or removal of any Agent or of any change by any Agent of its specified office;

o) if, before an Interest Payment Date for any Bond, it becomes subject generally to the taxing jurisdiction of any territory or any political sub-division thereof or any authority therein or thereof having power to tax other than or in addition to the United Kingdom, to notify (immediately upon becoming aware thereof) the Bond Trustee of such event and (unless the Bond Trustee otherwise agrees) to enter into a deed supplemental to the Bond Trust Deed, so that the relevant Condition shall make reference to that other or additional territory; and

p) to notify the Bond Trustee of any amendment to the Dealership Agreement.

Financial Covenants

(i) SWS has undertaken, among other things:

a) to deliver, with each Compliance Certificate and each Investors Report, a statement confirming that it has calculated each of the following ratios as at the Calculation Date immediately prior to the date of delivery of that Compliance Certificate, specifying the results of such calculations and providing a copy of the computations made in respect of the calculation of such ratios:

(A) the Class A ICR for each Test Period;

(B) the Senior Adjusted ICR for each Test Period;

(C) the Class A Adjusted ICR for each Test Period;

(D) the Senior Average Adjusted ICR;

(E) the Class A Average Adjusted ICR;

(F) the Senior RAR as at such Calculation Date and, in the case of forward-looking ratios, the 31 March falling in each Test Period;

(G) the Class A RAR as at such Calculation Date and, in the case of forward-looking ratios, the 31 March falling in each Test Period; and

(H) the ratio of Net Cash Flow minus Capital Maintenance Expenditure to Class A Debt Interest for the 12 month period ending on such Calculation Date,

and to calculate (x) the historical ratios using the audited financial statements (or unaudited financial statements if audited financial statements are not available on such date) delivered with such Compliance Certificate and (y) the forward-looking ratios using the SWS Business Financial Model which shall be prepared on a consistent basis and using assumptions from the most recently available relevant information and the most recently delivered financial statements; and

b) at each Periodic Review and on making each IDOK application, to apply to the Director General for a price determination which in the reasonable opinion of the SWS directors would allow, at a minimum, a credit rating in the A Category to be achieved and maintained for the Class A Unwrapped Debt and a shadow rating in the A Category to be achieved and maintained for the Class A Wrapped Debt, in each case from at least two of the Rating Agencies.

(ii) The Issuer has further undertaken to maintain:

a) a DSR Liquidity Facility available for drawing which (when aggregated with all amounts (including the value of any Authorised Investments) standing to the

credit of the Debt Service Reserve Account) is not less than the amount of interest (including Lease Reserve Amounts and Adjusted Lease Reserve Amounts) payable on its Class A Debt and Class B Debt for the next succeeding 12 month period (after taking into account the impact on interest rates of such Class A Debt and Class B Debt of any Hedging Agreements then in place); and

b) an O&M Reserve and/or O&M Reserve Facility available for drawing which together (including the value of any Authorised Investments funded from the balance on any O&M Reserve Account) amount to not less than 10 per cent. of Projected Operating Expenditure and Capital Maintenance Expenditure for the next succeeding 12 month period as forecast in the SWS Business Financial Model.

Trigger Events

The Common Terms Agreement also sets out certain Trigger Events. The specific Trigger Events and the consequences which flow from the occurrence of those events are set out below.

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

(i) Financial Ratios

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

a) the Senior RAR as at such Calculation Date or, in the case of forward-looking ratios, as at 31 March falling in any Test Period is or is estimated to be more than 0.900:1;

b) the Class A RAR as at such Calculation Date or, in the case of forward-looking ratios, as at 31 March falling in any Test Period is or is estimated to be more than 0.750:1;

c) the Senior Adjusted ICR for any Test Period is or is estimated to be less than 1.10:1;

d) the Class A Adjusted ICR for any Test Period is or is estimated to be less than 1.30:1;

e) the Senior Average Adjusted ICR is or is estimated to be less than 1.20:1; or

f) the Class A Average Adjusted ICR is or is estimated to be less than 1.40:1.

(ii) Credit Rating Downgrade

a) The long-term shadow credit rating of any Class A Wrapped Debt given by any two of the Rating Agencies falls to BBB (S&P), Baa2 (Moody's) or BBB (Fitch) or below;

b) the long-term credit rating of any Class A Unwrapped Debt by any two of the Rating Agencies falls to BBB (S&P), Baa2 (Moody's) or BBB (Fitch) or below;

c) the long-term shadow credit rating of the Class B Wrapped Debt by any two of the Rating Agencies falls below Investment Grade; or

d) the long-term credit rating of the Class B Unwrapped Debt by any two of the Rating Agencies falls below Investment Grade.

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

(iii) Debt Service Payment Account Shortfall

The failure by SWS to pay the Monthly Payment Amount within five Business Days following the date on which such payment was scheduled to be made.

(iv) Material Deviation in Projections

On any Calculation Date, the estimated actual Capital Expenditure over any five year period between Periodic Reviews exceeds the Capital Expenditure for that period assumed by the Director General in the last Periodic Review (adjusted to take account of any subsequent IDOK and Out-turn Inflation, including variances in real construction prices from assumed construction prices, and deducting capital expenditure incurred or to be incurred in respect of items for which SWS is entitled to make an application for an IDOK) in respect of SWS by 10 per cent. or more.

(v) Liquidity for Capital Expenditure and Working Capital

If, as at any Calculation Date, the aggregate of (i) SWS' operating cash flows including monies standing to the credit of the Operating Accounts available or forecast to be available to meet Capital Expenditure and working capital requirements for the next Test Period; (ii) Authorised Credit Facilities (excluding Liquidity Facilities) available to be drawn in the next 12 month period; and (iii) all amounts standing to the credit of the Capex Reserve Account is less than the aggregate of SWS' (a) forecast Capital Expenditure projected for the next 12 month period; (b) forecast working capital requirements projected for the next 12 month period; (c) the maximum total amount of interest in respect of Class A Debt and Class B Debt which is or is projected to fall due and payable during the next succeeding 12 month period; (d) all amounts which are or are projected to fall due and payable during the next succeeding 12 month period in respect of Financial Indebtedness which falls within paragraph (e) of the definition of Permitted Financial Indebtedness; and (e) the amount the Issuer estimates, in its reasonable opinion,

is equal to the net amount payable by the Issuer to a Hedge Counterparty following the exercise of an option to terminate a Treasury Transaction as permitted by the Hedging Policy.

(vi) Drawdown on DSR Liquidity Facilities and O&M Reserve Facility

If, at any time, the aggregate of all amounts available for drawing under the DSR Liquidity Facilities and all amounts standing to the credit of the Debt Service Reserve Account is less than the Required Balance (although it will not be a Trigger Event if it is triggered as a direct result of a banking error and remedied by such amount being repaid within three Business Days without such repayment being funded by a further drawing under a DSR Liquidity Facility).

The Issuer draws down under an O&M Reserve Facility or either the Issuer or SWS withdraws funds from either O&M Reserve Account, in either case to pay SWS' operating or maintenance expenditure (excluding any drawing or repayment of any Standby Drawing in relation to the Issuer's O&M Reserve Facility).

(vii) Enforcement Order

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

(viii) Circumstances leading to a Special Administration Order

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

(ix) Termination of Instrument of Appointment

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

(x) Event of Default

An Event of Default is continuing.

(xi) Material Entity Event.

A Material Entity Event occurs in relation to a Material Agreement or a Contractor and/or SWS under a Material Agreement and which continues unremedied for 60 days (other than (i) a Material Entity Event in relation to a Contractor's failure to pay (see paragraph (a) of "*Material Entity Events*" below) which continues unremedied for 45 days or (ii) a Material Entity Event in relation to a misrepresentation or breach of obligation which is capable of remedy (see paragraphs (b) and (c) of "*Material Entity Events*" below) which continues unremedied for 30 days) from the date from which SWS could be reasonably

expected to become aware of such Material Entity Event unless the relevant Contractor has been replaced in accordance with the Outsourcing Policy or SWS has terminated the appointment of the relevant Contractor and assumed the obligations of the Contractor under the relevant Material Agreement.

(xii) Referral

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

(xiii) Audit Qualification

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

(xiv) Adverse Governmental Legislation

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

(xv) Modification or Replacement of Instrument of Appointment

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

(xvi) Conduct of Business

The Permitted Non-Appointed Business Limits are breached.

(xvii) Breach of Outsourcing Policy

SWS fails duly to perform or comply with its material obligations as required under the Outsourcing Policy (other than as a result of Permitted Emergency Action) and fails to remedy such breach within 90 days of SWS becoming aware of such breach. (In March 2005 SWS obtained a waiver from the Majority Creditors in relation to certain aspects of

the Single Entity Contract described in Chapter 4 (*Description of the SWS Financing Group – Capital Investment Programme*) that do not comply with the Outsourcing Policy.)

(xviii) Adverse Final Determination of K

A final determination of K by Ofwat which is reasonably likely to have a Material Adverse Effect.

(xix) Shareholder Tax Deed of Covenant

A TDC Breach arises under the Shareholder Tax Deed of Covenant solely as a result of the acquisition by a person of control of SWSGH by virtue of acquiring a beneficial interest in any shares in RBSG.

Trigger Event Consequences

Following the occurrence of a Trigger Event and at any time until such Trigger Event has been waived by the Security Trustee, remedied in accordance with Trigger Event Remedies (see "*Trigger Events Remedies*" below) or otherwise remedied to the satisfaction of the Security Trustee, the following consequences ("**Trigger Event Consequences**") will apply:

(i) No Restricted Payments

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

(ii) Further Information and Remedial Plan

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

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

(iii) Independent Review

a) The Security Trustee may (acting on the instructions of the Majority Creditors) commission an Independent Review to be undertaken on the timetable stipulated by the Security Trustee. The Independent Review will be conducted by technical advisers to the Security Trustee appointed from time to time or such other person as the Security Trustee may decide.

b) The Independent Review will examine the causes of the relevant Trigger Event and recommend appropriate corrective measures.

c) Each of the Issuer and SWS must co-operate with the person appointed to prepare the Independent Review including providing access to its books and records and personnel and facilities as may be required for those purposes.

(iv) Consultation with Ofwat

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

(v) Appointment of additional non-executive directors

If the relevant Trigger Event has not otherwise been remedied or waived within six months from the date of its occurrence or such longer period as the Security Trustee, each Financial Guarantor and SWS may agree in a Remedial Plan, the Security Trustee will be entitled to procure the appointment of further non-executive directors to the board of SWS (in addition to those already on the board of SWS) in such numbers as would allow it, following such appointments, to have appointed a maximum of 20 per cent. of the board by number.

(vi) Payments under Outsourcing Agreements and Capex Contracts with Associates

All payments made by SWS under Outsourcing Agreements and/or Capex Contracts with Associates (excluding, for the avoidance of doubt, contracts which fall within paragraphs (a) and (c) of the definition of Distribution) which do not comply with the Outsourcing Policy in all material respects, shall be made as Distributions where such non-compliance has remained unremedied for a period in excess of 365 days from the date on which SWS became aware of such non-compliance.

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

Trigger Event Remedies

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

The following shall constitute remedies to the Trigger Events (each, a "**Trigger Event Remedy**"):

(i) Financial Ratios

The breach of a Trigger Event Ratio Level shall be remedied if such ratio or ratios come within the relevant level or levels specified below in relation to the most recently occurring Calculation Date:

a) the Senior RAR as at such Calculation Date and, in the case of any forward-looking ratios, as at the 31 March falling in each Test Period relating to such Calculation Date is or is estimated to be less than 0.900:1;

b) the Class A RAR as at such Calculation Date and, in the case of any forward-looking ratios, as at the 31 March falling in each Test Period relating to such Calculation Date is or is estimated to be less than 0.750:1;

c) the Senior Adjusted ICR for each Test Period relating to such Calculation Date is or is estimated to be greater than 1.10:1;

d) the Class A Adjusted ICR for each Test Period relating to such Calculation Date is or is estimated to be greater than 1.30:1;

e) the Senior Average Adjusted ICR is or is estimated to be greater than 1.20:1; or

f) the Class A Average Adjusted ICR is or is estimated to be greater than 1.40:1.

(ii) Credit Rating Downgrade

The occurrence of a Trigger Event in relation to a credit rating downgrade (see paragraph (ii) of "*Trigger Events*" above) shall be remedied if the credit rating of the relevant Class of debt given by any two of the Rating Agencies is above the Trigger Credit Rating.

(iii) Debt Service Required Payment Shortfall

The occurrence of a Trigger Event in relation to the non-payment of the Monthly Payment Amount into the Debt Service Payment Account (see paragraph (iii) of "*Trigger Events*" above) will be remedied if payment of the required amount is paid into the Debt Service Payment Account.

(iv) Material Deviation in Projections

The occurrence of a Trigger Event in relation to material deviations in projections (see paragraph (iv) of "*Trigger Events*" above) will be remedied if the deviations referred to in that paragraph, on any subsequent date, are less than 10 per cent. of the figure assumed by the Director General in the last Periodic Review (adjusted to take account of any subsequent IDOK and Out-turn Inflation) or, if a different figure is subsequently agreed

by Ofwat and SWS, the deviations are less than 10 per cent. of the subsequently agreed figure, as the case may be.

(v) Liquidity for Capital Expenditure and Working Capital

The occurrence of a Trigger Event in relation to liquidity for capital expenditure and working capital (see paragraph (v) of "*Trigger Events*" above) will be remedied if on any subsequent date the amounts referred to in sub-paragraphs (i) to (iii) of that paragraph are in aggregate equal to or greater than the aggregate of the amounts referred to in sub-paragraphs (a) to (e) of that paragraph.

(vi) Drawdown on DSR Liquidity Facilities and O&M Reserve Facility

a) The occurrence of a Trigger Event in relation to drawdowns under the DSR Liquidity Facility (see paragraph (vi) of "*Trigger Events*" above) will be remedied if the amount available for drawing under the DSR Liquidity Facilities when aggregated with all amounts standing to the credit of the Debt Service Reserve Account is restored to at least the Required Balance.

b) The occurrence of a Trigger Event in relation to a drawing under the O&M Reserve Liquidity Facility (see paragraph (vi) of "*Trigger Events*" above) will be remedied if the amount available for drawing under the O&M Reserve Facility, when aggregated with the O&M Reserve, is at least equal to the O&M Reserve Required Amount.

(vii) Enforcement Order

The occurrence of a Trigger Event in relation to an Enforcement Order (as set out in paragraph (vii) of "*Trigger Events*" above) will be remedied if SWS has complied with the terms of the relevant Enforcement Order to the reasonable satisfaction of the Security Trustee or if the Enforcement Order has been effectively withdrawn or if, in the opinion of the Security Trustee (acting reasonably), the relevant fine will not have a Material Adverse Effect or that the Instrument of Appointment will not be terminated.

(viii) Circumstances leading to a Special Administration Order

The occurrence of a Trigger Event in relation to circumstances leading to a Special Administration Order (as set out in paragraph (viii) of "*Trigger Events*" above) will be remedied if (a) a Special Administration Order is not made within six months of the relevant Trigger Event occurring or (b) the Security Trustee is reasonably satisfied that a Special Administration Order will not be made in respect of SWS.

(ix) Termination of Instrument of Appointment

The occurrence of a Trigger Event in relation to termination of the Instrument of Appointment (as set out in paragraph (ix) of "*Trigger Events*" above) will be remedied by agreement by SWS to the extent that a Transfer Scheme reasonably satisfactory to the

Security Trustee is implemented prior to the termination of the Instrument of Appointment.

(x) Event of Default

The occurrence of a Trigger Event in relation to an Event of Default (as set out in paragraph (x) of "*Trigger Events*" above) will be remedied if the Event of Default is waived or revoked in accordance with the STID or is remedied to the reasonable satisfaction of the Security Trustee.

(xi) Material Entity Event

The occurrence of a Material Entity Event in relation to a Material Entity Event (as set out in paragraph (xi) of "*Trigger Events*" above) will be remedied:

a) if it is remedied to the satisfaction of the Security Trustee and each Financial Guarantor;

b) if the Contractor has been replaced in accordance with the Outsourcing Policy or if SWS has terminated the appointment of the relevant Contractor and assumed the obligations of that Contractor as prescribed under the relevant Material Agreement; or

c) upon the acceptance by the Security Trustee and each Financial Guarantor of a Remedial Plan for as long as it is being complied with in all respects.

(xii) Referral

The occurrence of a Trigger Event in relation to a referral under the Instrument of Appointment (as set out in paragraph (xii) of "*Trigger Events*" above) will be remedied if:

a) in the absence of any determination or forecast of the determination of the Director General the financial ratios set out above come within the relevant level or levels specified in paragraph (i) of "*Trigger Event Remedies*" in relation to the most recently occurring Calculation Date; or

b) the Director General has made a determination that restores the financial ratios specified in paragraph (i) of "*Trigger Events*" above to at least the Trigger Event Ratio Levels.

(xiii) Audit Qualification

The occurrence of a Trigger Event in relation to an audit qualification (as set out in paragraph (xiii) of "*Trigger Events*" above) will be remedied if the Security Trustee is satisfied that such qualification does not affect the veracity of the financial ratios calculated in accordance with the Common Terms Agreement or if SWS produces a further set of Statutory Accounts upon which the auditors' report is not qualified.

(xiv) Adverse Governmental Legislation

The occurrence of the Trigger Event in relation to adverse Governmental legislation (as set out in paragraph (xiv) of "*Trigger Events*" above) will be remedied if the draft bill fails to become an act of parliament or becomes an act in a form which is reasonably likely not to cause a breach of the financial ratios set out in paragraph (i) of "*Trigger Events*" above or such financial ratios are otherwise reinstated to the Trigger Event Ratio Levels or the Director General has confirmed that the Capital Expenditure which would otherwise have led to a material deviation as referred to in paragraph (iv) of "*Trigger Events*" above is allowable under adjustments to the RCV and, when taking such adjustment into account, such financial ratios would meet the Trigger Event Ratio Levels.

(xv) Modification or Replacement of Instrument of Appointment

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

a) have a Material Adverse Effect; or

b) result in a breach of the financial ratios as referred to in paragraph (i) of "*Trigger Events*" above.

(xvi) Conduct of Business

Within six months of the date of the occurrence of the Trigger Event in relation to the conduct of business (as set out in paragraph (xvi) of "*Trigger Events*" above), SWS disposes of all or part of the Permitted Non-Appointed Business so that the Permitted Non-Appointed Business Limits will be complied with during the current Test Period excluding (for the purpose of calculating such ratio) the aggregate Non-Appointed Expenses of the former Permitted Non-Appointed Business which has been disposed of by SWS during such Test Period.

(xvii) Breach of Outsourcing Policy

The occurrence of the Trigger Event in relation to a breach of the Outsourcing Policy (as set out in paragraph (xvii) of "*Trigger Events*" above) will be remedied and the Trigger Event Consequence set out in paragraph (vi) of "*Trigger Event Consequences*" above will be disapplied if SWS takes such action as is necessary so that it is in compliance with the Outsourcing Policy.

(xviii) Adverse Final Determination of K

The occurrence of the Trigger Event in relation to an adverse final determination of K (as set out in paragraph (xviii) of "*Trigger Events*" above) will be remedied if the financial ratios set out above 'come within the relevant level or levels specified in paragraph (i) of "*Trigger Event Remedies*" in relation to the most recently occurring Calculation Date.

(xix) Shareholder Tax Deed of Covenant

The occurrence of a Trigger Event in relation to the Shareholder Tax Deed of Covenant as set out in paragraph (xix) under "*Trigger Events*" above will be remedied if either:

a) the circumstances which gave rise to the TDC Breach referred to in that paragraph cease to exist; or

b) the Security Trustee confirms pursuant to the Shareholder Tax Deed of Covenant that the TDC Breach which caused the Trigger Event is no longer occurring.

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

Events of Default

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

(a) non-payment of amounts payable under the Finance Documents within three Business Days of the due date;

(b) non-compliance with certain other obligations under the Finance Documents (other than the Tax Deeds of Covenant) or the occurrence of a TDC Breach which is continuing;

(c) material misrepresentation;

(d) any Financial Indebtedness not being paid when due (after the expiry of any applicable grace period) or any Financial Indebtedness being declared due and payable prior to its specified maturity as a result of an event of default;

(e) an Insolvency Event or Insolvency Proceedings occur(s) in relation to the Obligors other than SWS or, in relation to SWS, an insolvency event or insolvency proceedings as set out further in the CTA occur(s) in relation to SWS;

(f) SWS transferring the Instrument of Appointment without the Security Trustee's consent or SWS receiving notice that the Instrument of Appointment will be revoked or

terminated and a scheme of transfer not being approved by the Secretary of State or the Director General on or before the date falling two years prior to the expiration of such notice;

(g) the Instrument of Appointment being terminated and not replaced immediately by a further licence on equivalent terms taking into account any changes in the regulatory environment since the Initial Issue Date;

(h) insufficient liquidity (from operating cash flows, the Authorised Credit Facilities and the Capex Reserve Account) to meet SWS' forecast Capital Maintenance Expenditure and working capital requirements projected for the next six month period;

(i) attachment, sequestration, distress or execution involving sums in excess of £500,000 (indexed) and if not discharged within 30 days;

(j) any Obligor repudiating a Finance Document or it becoming unlawful or ineffective for any Obligor to perform its material obligations under any Finance Document;

(k) an SWS Change of Control occurs;

(l) any of the Security ceasing to be in full force and effect;

(m) certain governmental action (including nationalisation) which would be reasonably likely to have a Material Adverse Effect;

(n) a member of the SWS Financing Group failing to comply with a judgment involving sums in excess of £500,000 (indexed) in aggregate at any time except where such judgement is being appealed in good faith to a higher court;

(o) other than in the case of a Permitted Lease Termination, an Obligor not having legal power to perform its obligations under the Finance Documents or any obligation of any Obligor under a relevant Finance Document (other than stamp duty indemnities) ceasing to be legal, binding and enforceable and the absence of compliance has a Material Adverse Effect;

(p) SWS failing to comply with its obligations under the Outsourcing Policy (and such failure has a Material Adverse Effect);

(q) an Obligor other than SWS ceasing or threatening to cease to carry on its business (or any substantial part of its business) it carries on as at the date of the CTA or as contemplated by the Finance Documents or SWS ceasing or threatening to cease to carry on the Appointed Business (or any substantial part of the Appointed Business) it carries on at the date of the CTA or which is contemplated by the Finance Documents other than as permitted by the Finance Documents;

(r) litigation being started against an Obligor or its assets or revenues which would be reasonably likely to be adversely determined and, if so adversely determined, would have a Material Adverse Effect;

(s) the shadow rating of the Class A Wrapped Bonds or the rating of the Class A Unwrapped Bonds in each case ascribed by two Rating Agencies being less than the minimum required for Investment Grade;

(t) the Class A ICR being less than 1.60:1, the Senior RAR being more than 0.950:1 and/or the ratio of Net Cash Flow minus Capital Maintenance Expenditure to Class A Debt Interest for the immediately preceding 12 month period is less than 1.00:1;

(u) an Obligor (other than SWS) amending its memorandum or articles of association or SWS amending its memorandum or articles, if such amendment relates to the terms of the SWS Preference Shares or is in a manner which is reasonably likely to have a Material Adverse Effect or diminish the value of any Security Interest granted in favour of the Security Trustee, unless the Security Trustee has previously given its prior written consent to such amendment;

(v) a Material Entity Event (as described in "*Material Entity Events*" below) occurring which has a Material Adverse Effect.

In March 2005 SWS obtained a waiver from the Majority Creditors in relation to certain aspects of the Single Entity Contract described in Chapter 4 (*Description of the SWS Financing Group – Capital Investment Programme*) that do not comply with the Outsourcing Policy.

In June 2005, SWS obtained a waiver from the Majority Creditors to allow it to enter into certain Hedging Agreements in connection with the Second Revolving Credit Facility. The Majority Creditors approved an extension of such waiver in April 2006.

In December 2005, SWS obtained a waiver from the Majority Creditors in relation to the opening of two new bank accounts required in order to implement a counter payment network service administered by PayPoint Network Limited and PayPoint Collections Limited, which provides SWS with the facility to collect cash payments for water bills through PayPoint terminals located in the convenience retail sector.

SWS has obtained waivers from the Majority Creditors in respect of the requirement to produce consolidated accounts for SWS for the years ending 31 march 2005 and 31 March 2006.

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

Immediately upon the notification to the Security Trustee of an occurrence of an Event of Default, a Standstill Period will commence in accordance with the STID (see "*Security Trust and Intercreditor Deed — Standstill*" above).

Material Entity Events

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

(a) any amount due from the Contractor or SWS is not paid unless payment is made within 15 days of an Obligor becoming aware of such failure or save if such payment is being disputed in good faith;

(b) any representation or statement made or deemed to be made by a Contractor or SWS in any Material Agreement is or proves to have been incorrect or misleading in any respect when made or deemed to be made and such failure, if capable of remedy, is not remedied by the Contractor or SWS within 30 days of it becoming aware that such representation was incorrect or misleading in any respect;

(c) the Contractor or SWS fails duly to perform or comply with any other obligation expressed to be assumed by it in any Material Agreement and such failure, if capable of remedy, is not remedied by such Contractor or SWS, as the case may be, within 30 days of becoming aware of such breach;

(d) the Contractor:

 (A) ceases or suspends generally payment of its debts or publicly announces an intention to do so or is unable to pay its debts as they fall due or is deemed to be insolvent; or

 (B) commences negotiations with or makes a proposal to any one or more of its creditors concerning its solvency, with a view to the readjustment or rescheduling of any indebtedness;

(e) an Insolvency Event or equivalent event occurs in relation to a Contractor to a Material Agreement;

(f) the Contractor fails to comply with or pay any sum due from it under any judgment or any order made or given by any court of competent jurisdiction at any time except where such judgment is being appealed in good faith to a higher court;

(g) any Material Agreement to which the Contractor and SWS is a party or any obligation purported to be contained therein or the security or credit enhancement intended to be effected in relation to such Material Agreement is repudiated by the Contractor or SWS or it does or causes to be done any act or thing evidencing an intention to repudiate, abandon, cancel, suspend or terminate any Material Agreement to which SWS or the Contractor is a party or the security or credit enhancement related there to or any such obligation or any such security or subordination effected under any of the Material Agreements to which it is a party or any Material Agreement is not or ceases to be in full force and effect or the legal validity or applicability thereof to any sums due or to become

due thereunder is disaffirmed by the Contractor or SWS or on behalf of the Contractor or SWS; and

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

Conditions Precedent

The conditions precedent to, among other things, the release of Financial Guarantees and to the issue of Bonds are set out in a conditions precedent agreement dated 23 July 2003 (the "**CP Agreement**") between, among others, the Bond Trustee, the Security Trustee and the Obligors.

Cash Management

Accounts

In accordance with the Common Terms Agreement, SWS has opened and maintains the following Accounts with the Account Bank:

(a) each Operating Account;

(b) an O&M Reserve Account; and

(c) the Capex Reserve Account.

The Issuer has also opened or (in the case of the O&M Reserve Account) shall open and maintain the following Accounts with the Account Bank:

(a) the Debt Service Payment Account;

(b) the Debt Service Reserve Account; and

(c) in the event the Issuer becomes a borrower under an O&M Reserve Facility, an O&M Reserve Account.

SWSGH and SWSH have each opened and maintain one chequing account only with the Account Bank.

Each of the above accounts together with any other bank account of any Obligor are collectively referred to as the "**Accounts**". Each of the Accounts is held with the Account Bank pursuant to the Account Bank Agreement. Each Obligor agreed in the Common Terms Agreement to comply

with the Account Bank Agreement and the provisions of the Common Terms Agreement applying to its Accounts.

Operating Accounts

Under the Common Terms Agreement, SWS must ensure that all of its revenues (other than any interest or Income which is credited to the Account from which the Authorised Investment was made) will be paid into an operating account.

For those revenues of SWS which are received into existing collection accounts of SWS with a bank other than the Account Bank, SWS must ensure the balance on such collection accounts is transferred into an Operating Account at least once a week and, following a downgrade of the short term unsecured unsubordinated debt rating of such bank (excluding for this purpose Alliance & Leicester Commercial Bank plc (formerly Girobank)) below the Minimum Short-term Rating, on close of business of each Business Day.

The Operating Accounts are the principal current accounts of SWS through which all operating and Capital Expenditure or any Taxes incurred by SWS and (subject to the terms of the Finance Documents) payments in respect of the Financial Indebtedness of the SWS Financing Group which are not permitted to be satisfied out of monies credited to the Debt Service Payment Account are cleared. SWS may make transfers at any time from one Operating Account to another, in its sole discretion.

All operating expenditure of SWS is funded (a) through payments made directly into the Operating Accounts and (b) through drawings made by the Issuer or SWS under any Authorised Credit Facility or other Permitted Financial Indebtedness and, in the case of drawings made by the Issuer (except under any DSR Liquidity Facility), on lent to SWS under an Issuer/SWS Loan Agreement, as and when required and permitted by the Finance Documents. Capital Expenditure is funded out of monies standing to the credit of the Operating Accounts, out of cash transfers made from the Capex Reserve Account to the Operating Accounts and/or (in relation to Capital Maintenance Expenditure), to the extent that the sums standing to the credit of the Operating Accounts and the Capex Reserve Account are insufficient, SWS' O&M Reserve Account.

All Distributions, payments under the SWS Preference Shares (or, following an SWS Preference Share Conversion Event, the relevant Subordinated Debt into which the SWS Preference Shares are converted) and Permitted Post-Closing Events have been or will be funded (directly or indirectly) out of monies standing to the credit of the Operating Accounts subject always to the satisfaction of all of the conditions set out in the Common Terms Agreement for the making of such payments.

Annually on 31 March of each year (or, if such day is not a Business Day, the immediately preceding Business Day) SWS calculates the Annual Finance Charge for the period of 12 months commencing on the immediately following 1 April, and details of such calculation are included in the next following Investors Report.

Under the Common Terms Agreement, SWS on the opening of business on the first Business Day of each month until the Discharge Date transfers to the Issuer from the Operating Accounts an amount (the "**Monthly Payment Amount**") equal to 1/12th of SWS' Annual Finance Charge

for the relevant 12 month period to the Debt Service Payment Account provided that the aggregate of any interest accruing on and credited to the Debt Service Payment Account is treated as a prepayment of future Monthly Payment Amounts payable during the relevant 12 month period. Accordingly, the Monthly Payment Amounts due for the remaining months of such 12 month period shall be reduced pro rata to reflect such prepayment.

SWS recalculates the Annual Finance Charge and the Monthly Payment Amount, as applicable if, during the course of any relevant 12 month period, there occurs any increase (whether as a result of any increase in the rate of applicable interest, any drawing under any Authorised Credit Facility, any deferral of interest, any upwards adjustment of rentals under any Finance Lease, or otherwise) or decrease (whether as a result of any reduction in the rate of applicable interest, downwards adjustment of rentals under any Finance Lease or any prepayment or repayment of the debt under which the relevant liabilities arise or accrue or otherwise) in the Annual Finance Charge and adjusts the Monthly Payment Amount for the remaining months in the relevant 12 month period, and details are included in the next following Investors Report.

Capex Reserve Account

As at 31 March 2006 approximately £195.1 million was standing to the credit of the Capex Reserve Account.

SWS may not withdraw any monies from the Capex Reserve Account unless such withdrawal is for the purpose of funding a transfer to the Operating Account on account of SWS' capital expenditure requirements or as contemplated below in relation to the application of insurance proceeds.

SWS must ensure that the proceeds of any advance to it under any Authorised Credit Facility for the purpose of funding its capital expenditure is paid directly into the Capex Reserve Account or an Operating Account.

SWS must also ensure that all proceeds of any property damage insurance claim (other than in respect of delay in start up, business interruption or anticipated loss in revenue or third party claims) are paid directly into the Capex Reserve Account.

SWS may withdraw the proceeds of property damage insurance claims from the Capex Reserve Account for application in meeting payments which are due and payable in respect of the restoration, reinstatement or replacement of the asset lost or damaged or, where any Permitted Lease Termination has arisen as a consequence of the loss of such asset, in payment of any Class A Debt falling due on the date of that Permitted Lease Termination arising as a consequence of the loss of such asset.

If SWS has paid sums to reinstate, restore or replace assets or effects lost or damaged or to meet claims by third parties out of moneys withdrawn from the Operating Accounts, then SWS may pay the relevant insurance amounts received directly into an Operating Account. If the reinstatement, restoration or replacement cost of any damaged property is less than the property damage insurance proceeds received by it in relation to such property, SWS may pay the difference into an Operating Account.

SWS' O&M Reserve Account

As at 31 March 2006 approximately £44.1 million was standing to the credit of the O&M Reserve Account.

SWS may not withdraw any monies from its O&M Reserve Account unless (i) such withdrawal is for the purpose of funding a transfer to an Operating Account on account of operating and capital expenditure requirements that cannot be met from existing balances in the Operating Accounts and additionally, in the case of any capital expenditure requirement, the Capex Reserve Account (ii) such withdrawal is for the purpose of transferring into an Operating Account any interest income earned from time to time on the O&M Reserve (including Income from any related Authorised Investments) or (iii) prior to making a withdrawal, SWS delivers a certificate to the Security Trustee and the Account Bank certifying that, following such proposed withdrawal, the aggregate of the O&M Reserve and all amounts then available for drawing under any O&M Reserve Facility are at least equal to the O&M Reserve Required Amount on the date of such withdrawal. As at the date of this Prospectus, SWS has not withdrawn any monies from its O&M Reserve Account.

SWS must ensure that the proceeds of any drawing by the Issuer under any O&M Reserve Facility Agreement (other than a Standby Drawing) are lent by the Issuer to SWS under an Issuer/SWS Loan Agreement and are paid directly into SWS' O&M Reserve Account or an Operating Account.

Debt Service Payment Account

As at 31 March 2006 approximately £1.8 million was standing to the credit of the Debt Service Payment Account.

SWS must ensure that each transfer of or in respect of the Monthly Payment Amount from the Operating Account, is made to the Issuer directly into the Debt Service Payment Account.

The Common Terms Agreement provides that, on each Payment Date, monies credited to the Debt Service Payment Account must be applied by the Issuer in the following order for the purpose of enabling the following payments ("**Permitted Payments**") to be made in the following order of priority (the "**Payment Priorities**") without double counting:

(i) *first* (to the extent there are insufficient monies standing to the credit of all other Accounts and/or available for drawing under any Liquidity Facility), in or towards satisfaction of all of the SWS Financing Group's operating costs (except to the extent falling due under the Finance Documents) and maintenance costs;

(ii) *second,* pro rata, according to the respective amounts thereof in or towards satisfaction of the remuneration, costs and expenses of the Security Trustee and the Bond Trustee;

(iii) *third*, pro rata, according to the respective amounts thereof in or towards satisfaction of, on a pro rata basis: (a) the remuneration, costs and expenses of each Agent, the Account Bank under the Account Bank Agreement, each DSR Liquidity Facility Provider under the relevant DSR Liquidity Facility Agreement, each O&M Reserve Facility Provider

under the relevant O&M Reserve Facility Agreement, each facility agent under the relevant Authorised Credit Facility and the Standstill Cash Manager; and (b) the remuneration, costs and expenses of and fees of each Financial Guarantor pursuant to the relevant G&R Deed;

(iv) *fourth*, pro rata according to the respective amounts thereof, in or towards satisfaction of: (a) all amounts of fees, interest and principal (other than any Subordinated Liquidity Facility Amounts) due or overdue to each DSR Liquidity Facility Provider under the relevant DSR Liquidity Facility Agreement; (b) all amounts of fees, interest and principal (other than Subordinated Liquidity Facility Amounts) due or overdue to each O&M Reserve Facility Provider under the relevant O&M Reserve Facility Agreement; and (c) all amounts of interest and principal due or overdue to each Authorised Credit Provider under the relevant Authorised Credit Facility to the extent that the Financial Indebtedness was incurred to fund a New Money Advance;

(v) *fifth*, pro rata according to the respective amounts thereof, in or towards satisfaction of all scheduled amounts payable to each Hedge Counterparty under any Interest Rate Hedging Agreement;

(vi) *sixth,* pro rata according to the respective amounts thereof, in or towards satisfaction of: (a) all amounts of interest (including the Lease Reserve Amounts and Adjusted Lease Reserve Amounts), recurring fees and commitment commissions due or overdue in respect of the Class A Debt (other than any Subordinated Coupon Amounts and Subordinated Authorised Loan Amounts); (b) any unscheduled amounts (including termination amounts) due and payable to each Hedge Counterparty under any Interest Rate Hedging Agreement (except to the extent required to be paid at paragraph (xvi) below); (c) all scheduled amounts (other than principal exchange amounts) payable to each Hedge Counterparty under any Currency Hedging Agreement in respect of Class A Debt and (subject to paragraph (xvi) below and following termination of a Standstill Period other than due to remedy or waiver by the Majority Creditors of, or the revocation of, the Event of Default giving rise to the Standstill Period) all amounts payable to each Hedge Counterparty under any Currency Hedging Agreement in respect of Class A Debt; (d) all amounts of underwriting commissions due or overdue in respect of the Class A Debt; and (e) all reimbursement sums (if any) owed to each Financial Guarantor under the relevant G&R Deed in respect of payments of interest on any Class A Wrapped Debt guaranteed by such Financial Guarantor;

(vii) *seventh*, pro rata according to the respective amounts thereof, in or towards satisfaction of: (a) all amounts of principal due or overdue in respect of the Class A Debt (including, in respect of Finance Leases, those amounts payable in respect thereof which do not fall within paragraph (vi) above and do not fall due as a result of the operation of any indemnity or fee reimbursement provision of a Finance Lease); (b) all principal exchange amounts due and payable to each Hedge Counterparty under any Currency Hedging Agreement in respect of Class A Debt; (c) any termination amounts or other unscheduled sums due and payable to each Hedge Counterparty under any Currency Hedging Agreement in respect of Class A Debt (except to the extent required to be paid at paragraph (xvi) below); and (d) all reimbursement sums (if any) owed to each Financial

Guarantor under the relevant G&R Deed in respect of payments of principal on any Class A Wrapped Debt guaranteed by such Financial Guarantor;

(viii) *eighth*, in or towards satisfaction of any Make-Whole Amount due and payable on the Class A Debt;

(ix) *ninth*, pro rata according to the respective amounts thereof, in or towards satisfaction of ail Subordinated Coupon Amounts due or overdue in respect of any Class A Bonds;

(x) *tenth,* in payment to the Debt Service Reserve Account until the sum of the balance thereon and the aggregate available commitments under the DSR Liquidity Facility Agreements is equal to the Class A Required Balance;

(xi) *eleventh*, in payment to the Issuer's O&M Reserve Account until the sum of the O&M Reserve and the aggregate of amounts available to be drawn under O&M Reserve Facilities is equal to the O&M Reserve Required Amount;

(xii) *twelfth*, pro rata according to the respective amounts thereof, in or towards satisfaction of all amounts of: (a) interest and commitment commissions due or overdue in respect of the Class B Debt (other than any Subordinated Coupon Amounts due or overdue in respect of any Class B Bonds and Subordinated Authorised Loan Amounts); (b) all amounts of underwriting commissions due or overdue in respect of the Class B Debt; (c) except to the extent required to be paid at paragraph (xvi) below, all scheduled amounts (other than principal exchange amounts) payable to each Hedge Counterparty under any Currency Hedging Agreement in respect of Class B Debt and (following termination of a Standstill Period other than due to remedy or waiver by the Majority Creditors of, or revocation of, the Event of Default giving rise to the Standstill Period) all amounts payable to each Hedge Counterparty under any Currency Hedging Agreement in respect of Class B Debt; and (d) all reimbursement sums (if any) owed to each Financial Guarantor under the relevant G&R Deed in respect of payments of interest on any Class B Wrapped Debt guaranteed by such Financial Guarantor;

(xiii) *thirteenth,* pro rata according to the respective amounts thereof, in or towards satisfaction of: (a) all amounts of principal due or overdue in respect of the Class B Debt; (b) all principal exchange amounts due and payable to each Hedge Counterparty under any Currency Hedging Agreement in respect of Class B Debt; (c) except to the extent required to be paid at paragraph (xvi) below, any termination amounts or other unscheduled sums due and payable to each Hedge Counterparty under any Currency Hedging Agreement in respect of Class B Debt; and (d) all reimbursement sums (if any) owed to each Financial Guarantor under the relevant G&R Deed in respect of payments of principal on any Class B Wrapped Debt guaranteed by such Financial Guarantor;

(xiv) *fourteenth,* pro rata according to the respective amounts thereof, in or towards satisfaction of any Make-Whole Amounts due and payable on the Class B Debt;

(xv) *fifteenth,* in payment to the Debt Service Reserve Account until the sum of the balance thereon and the aggregate available commitments under the DSR Liquidity Facilities is equal to the sum of the Class A Required Balance and the Class B Required Balance;

(xvi) *sixteenth*, pro rata according to the respective amounts thereof, in or towards satisfaction of: (a) any other amounts (not included in paragraphs (vi) and (vii) above) due and/or overdue to the Finance Lessors; and (b) any termination payment due or overdue to a Hedge Counterparty under any Hedging Agreement which arises as a result of a default by such Hedge Counterparty or as a result of a downgrade in the credit rating of such Hedge Counterparty (other than any amount attributable to the return of collateral or any premium or other upfront payment paid to the Issuer to enter into a transaction to replace a Hedging Agreement (in whole or in part)) shall be applied first in payment of amounts due to the Hedge Counterparty in respect of that Hedging Agreement;

(xvii) *seventeenth,* pro rata according to the respective amounts thereof, in or towards satisfaction of: (a) all Subordinated Liquidity Facility Amounts due or overdue to each Liquidity Facility Provider under the Liquidity Facility Agreements; (b) all Subordinated Authorised Loan Amounts due or overdue to each Authorised Credit Provider under the relevant Authorised Credit Facility in respect of Class A Debt; (c) any other indemnified amounts due or overdue to each Financial Guarantor under the relevant G&R Deed in respect of any Class A Wrapped Debt guaranteed by such Financial Guarantor; and (d) any amounts payable in respect of Class A Debt not referred to in other sub-paragraphs of the Payment Priorities;

(xviii) *eighteenth,* pro rata according to the respective amounts thereof, in or towards satisfaction of: (a) all Subordinated Authorised Loan Amounts due or overdue to each Authorised Credit Provider under the relevant Authorised Credit Facility in respect of Class B Debt; (b) any other indemnified amounts due or overdue to each Financial Guarantor under the relevant G&R Deed in respect of any Class B Wrapped Debt guaranteed by such Financial Guarantor; and (c) any amounts payable in respect of Class B Debt not referred to in any other sub-paragraphs of the Payment Priorities;

(xix) *nineteenth,* pro rata according to the respective amounts thereof, in or towards satisfaction of all Subordinated Coupon Amounts due or overdue in respect of any Class B Bonds;

(xx) *twentieth*, subject always to the satisfaction of the Restricted Payment Condition, pro rata according to the respective amounts thereof, in or towards satisfaction of all amounts of interest due or overdue in respect of the Senior Mezzanine Debt;

(xxi) *twenty-first,* subject always to the satisfaction of the Restricted Payment Condition, pro rata according to the respective amounts thereof, in or towards satisfaction of all amounts of principal due or overdue in respect of the Senior Mezzanine Debt;

(xxii) *twenty-second*, subject always to the satisfaction of the Restricted Payment Condition, pro rata according to the respective amounts thereof, in or towards satisfaction of any other sums due or overdue in respect of the Senior Mezzanine Debt;

(xxiii) *twenty-third*, subject always to the satisfaction of the Restricted Payment Condition, pro rata according to the respective amounts thereof, in or towards satisfaction of all amounts of interest due or overdue in respect of the Junior Mezzanine Debt;

(xxiv) *twenty-fourth*, subject always to the satisfaction of the Restricted Payment Condition, pro rata according to the respective amounts thereof, in or towards satisfaction of all amounts of principal due or overdue in respect of the Junior Mezzanine Debt;

(xxv) *twenty-fifth*, subject always to the satisfaction of the Restricted Payment Condition, pro rata according to the respective amounts thereof, in or towards satisfaction of any other sums due or overdue in respect of the Junior Mezzanine Debt;

(xxvi) *twenty-sixth*, subject always to the satisfaction of the Restricted Payment Condition, in or towards satisfaction of all sums due or overdue in respect of any Subordinated Debt into which the SWS Preference Shares have converted upon an SWS Preference Share Conversion Event where the holder of such Subordinated Debt has acceded to the STID as a Secured Creditor; and

(xxvii) *twenty-seventh*, (to the extent required in the Common Terms Agreement) the balance shall remain in the Debt Service Payment Account.

Any payment made by the Issuer to a Secured Creditor pursuant to the Payment Priorities on account of a liability in respect of which SWS is the principal debtor is treated as having discharged SWS' obligation to make such payment to that Secured Creditor. SWS is also treated as having discharged its related payment obligation to the Issuer under the relevant Issuer/SWS Loan Agreement upon (and to the extent of) the Issuer making a payment pursuant to the Payment Priorities to a Secured Creditor in respect of which the Issuer is the principal debtor.

The Payment Priorities set out in paragraphs (i) to (xxvi) inclusive do not apply to (a) the proceeds of any further borrowing of Permitted Financial Indebtedness which are required by the terms of such borrowing to be applied (i) in repayment or prepayment of any existing Financial Indebtedness of the SWS Financing Group (including Subordinated Debt) or (ii) in redeeming the SWS Preference Shares, in each case, to the extent permitted by the CTA or (b) any return of collateral or premium or up front payment in relation to a Hedging Agreement contemplated in paragraph (xvi) above which will be paid to the relevant Hedge Counterparty directly. In no circumstance is the Issuer entitled to apply monies represented by the Monthly Payment Amount in or towards making a Restricted Payment.

For so long as no Standstill Event is continuing, SWS must, on the date which is seven Business Days prior to each Payment Date (such date, a "**Determination Date**"), determine whether the aggregate amount of monies then credited to the Debt Service Payment Account is at least equal to the aggregate of all amounts referred to in paragraphs (i) to (xix) inclusive of the Payment Priorities which fall due and payable on such Payment Date taking account of any receipts due from any Hedge Counterparty under any Hedging Agreement on such Payment Date (such aggregate amount, "**Scheduled Debt Service**"). If the balance on the Debt Service Payment Account on a Determination Date is less than the amount of Scheduled Debt Service falling due on the following Payment Date, then SWS will promptly transfer to the Debt Service Payment Account an amount equal to the shortfall from sums standing to the credit of the Operating Accounts. No amounts may be so transferred to the extent that to do so would cause the aggregate net balance of the Operating Accounts to fall below the then current aggregate net overdraft limit on the Operating Accounts or cause the balance on any Operating Account to fall

below the then current gross overdraft limit in respect of such Operating Account. If after making any required transfers from the Operating Accounts the balance on the Debt Service Payment Account would be insufficient to pay any Scheduled Debt Service falling due for payment at items (i) to (vi), (ix) or (xii) of the Payment Priorities (excluding any termination payments under any Hedging Agreements), the Issuer must promptly request a drawing under the DSR Liquidity Facility for payment on the following Payment Date in an amount equal to the shortfall (subject to any limitations in the DSR Liquidity Facility Agreements on drawings applicable to shortfalls relating to Class B Debt).

Until such time as a Standstill commences and is continuing, all amounts payable on any Payment Date must be paid strictly in the order referred to above, to the intent that no amounts falling to be paid under any paragraph may be paid until such time as the amounts falling to be paid on the same date or earlier under each preceding paragraph have been paid in full.

Debt Service Reserve Account and Issuer's O&M Reserve Account

The Issuer will be required to drawdown the whole of a Liquidity Facility Provider's commitment if that Liquidity Facility Provider (i) ceases to have the Liquidity Facility Requisite Rating or (ii) fails to renew its commitment at the end of the term of the relevant Liquidity Facility and whose commitment is not replaced by another Liquidity Facility Provider. The Issuer must deposit the proceeds of each such drawdown into the Debt Service Reserve Account (in the case of a drawdown under a DSR Liquidity Facility Agreement) or the Issuer's O&M Reserve Account (in the case of a drawdown under any O&M Reserve Facility). No monies may be withdrawn from the Debt Service Reserve Account or the O&M Reserve Account except as permitted by the relevant Liquidity Facility Agreement (see the *"Liquidity Facilities"* below) or the Issuer delivers, prior to any withdrawal, a certificate to the Security Trustee and the Account Bank that following the making of such withdrawal (a) in the case of the Debt Service Reserve Account, the aggregate of the amounts standing to the credit of the Debt Service Reserve Account and available for drawing under the DSR Liquidity Facilities is at least equal to the Required Balance and (b) in the case of the Issuer's O&M Reserve Account, the aggregate of the O&M Reserve and amounts available for drawing under the O&M Facilities is at least equal to the O&M Required Amount.

SWS has agreed to procure that on any Payment Date (save for any date upon which a drawing is to be made under a DSR Liquidity Facility or out of the Debt Service Reserve Account to make a payment into the Debt Service Payment Account):

(a) the aggregate of (i) all amounts available for drawing under the DSR Liquidity Facilities; and (ii) all amounts standing to the credit of the Debt Service Reserve Account (including the value of any Authorised Investments) are equal to the next 12 months' interest forecast to be due on the Class A Debt of the SWS Financing Group (the **"Class A Required Balance"**); and

(b) the aggregate of (i) all amounts available for drawing in respect of Class B Debt under the DSR Liquidity Facilities; and (ii) all amounts standing to the credit of the Debt Service Reserve Account (including the value of any Authorised Investments) (after deducting all amounts required in order to satisfy the Class A Required Balance) are

equal to the next 12 months' interest forecast to be due on the Class B Debt (other than in respect of any Subordinated Coupon Amounts) of the SWS Financing Group (the **"Class B Required Balance"** and, together with the Class A Required Balance, the **"Required Balance"**).

Authorised Investments

The Common Terms Agreement allows SWS and the Issuer to invest in certain eligible Authorised Investments such part of the amounts standing to the credit of any of the Accounts as is prudent and in accordance with certain provisions to be set out in the Common Terms Agreement.

Cash Management during a Standstill Period

The arrangements described in *"Debt Service Payment Account"* above continue to apply until the commencement of a Standstill Period. The Common Terms Agreement provides that, so long as a Standstill Period continues unremedied, and provided no Enforcement Action (other than a Permitted Share Pledge Acceleration) has occurred, SWS shall cease to be the Cash Manager and will be replaced by the Standstill Cash Manager, who shall assume control of the Accounts, pay operating expenditure when it falls due and, on a monthly basis, calculate the aggregate of all payments falling to be made during the next following period of 12 months and shall calculate all net revenues received and/or expected to be received over that 12 month period. To the extent that the forecast revenues are insufficient (after paying all relevant operating expenditure) to pay the aggregate of all payments falling to be made during the next 12 months, the Standstill Cash Manager shall notionally apply those forecast revenues to each category in accordance with the Payment Priorities until the revenue that is forecast to be available is insufficient to meet all of the payments falling to be made within such 12 month period in any paragraph of the Payment Priorities (the **"Shortfall Paragraph"**) and shall, in respect of those categories of payment falling within the Shortfall Paragraph, divide the anticipated revenues remaining pro rata between those amounts. Throughout the Standstill Period, any payments falling to be made within a category of payment falling within a Shortfall Paragraph shall be satisfied by a payment of the pro rata share of that payment so calculated and no payments falling in a category which (in accordance with the Payment Priorities) falls after a Shortfall Paragraph shall be made (and the balance of the payments not made shall remain outstanding).

The proceeds of enforcement of the Security which is permitted to be enforced during a Standstill Period will also be applied in accordance with the Payment Priorities. In circumstances where such enforcement occurs during a Standstill Period or following termination of a Standstill the proceeds of enforcement will be applied in accordance with the above Payment Priorities but excluding in these circumstances payments under paragraphs (i), (x), (xi) and (xv) thereof.

Security Agreement

Security

Each Obligor entered into the security agreement (the **"Security Agreement"**) with the Security Trustee on the Initial Issue Date pursuant to which SWSH and SWSGH guarantee the obligations of each other Obligor under the Finance Documents and SWS and the Issuer guarantee the

obligations of each other under the Finance Documents, in each case to the Security Trustee as security trustee for the Secured Creditors. Each Obligor has secured its property, assets and undertakings to the Security Trustee as trustee for the Secured Creditors. However, in respect of SWS, the creation, perfection and enforcement of such security is subject to the WIA, the Instrument of Appointment and requirements thereunder. As a result of the restrictions placed upon SWS in respect of the giving of security and the Special Administration procedure contained in the WIA, the value, effect and enforceability of the security granted by SWS is severely limited (see Chapter 5 *"Risk Factors"* and Chapter 6 *"Water Regulation"* of this Prospectus for a more detailed discussion of these issues).

The Security Agreement incorporates, to the extent applicable, the provisions of the Common Terms Agreement and is subject to the STID.

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

(i) first fixed charges over:

a) the ordinary shares in SWS, SWSH, the Pension Companies and the Issuer;

b) each Obligor's right, title and interest from time to time in and to:

(A) any real property interests currently owned by it or acquired after the date of the Security Agreement (other than certain excluded property not exceeding in aggregate £10 million (indexed from the Initial Issue Date)); and

(B) the proceeds of disposal of any land (including Protected Land);

c) all present and future plant, machinery, office equipment, computers, vehicles and other chattels;

d) all moneys standing to the credit of each Obligor's accounts and the debts represented thereby;

e) any Intellectual Property Rights owned by each Obligor (excluding information technology licence agreements);

f) any present and future goodwill and any present and future uncalled capital and rights in relation to such uncalled capital;

g) each Authorised Investment;

h) all shares of any person owned by the Obligor including all dividends, interest and other monies payable in respect thereof and all other rights related thereto;

i) all present and future book and other debts;

j) all benefit in respect of Insurances taken out by any Obligor and all claims and returns of premiums in respect thereof; and

(ii) an assignment of each Obligor's right in respect of Insurances taken out by any Obligor and in respect of its right, title and interest from time to time in and to:

a) the proceeds of any insurance policies (other than motor insurance, employer's liability insurance, directors and officers liability insurance, pension fund trustee liability insurance and any other third party liability insurance) and all rights related thereto;

b) all Transaction Documents and any other document or agreement to which an Obligor is a party; and

c) all damages, compensation, remuneration, profit, rent or income derived from information technology licence agreements; and

(iii) a first floating charge of the whole of the undertaking, property, assets and rights whatsoever and wheresoever present and future of each Obligor, except that the Security does not include any security over Protected Land (see Chapter 6 *"Water Regulation"* under *"Protected Land"*) or any of SWS' other assets, property and rights to the extent, and for so long as, the taking of any such security would contravene the terms of the Instrument of Appointment and requirements thereunder or the WIA.

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

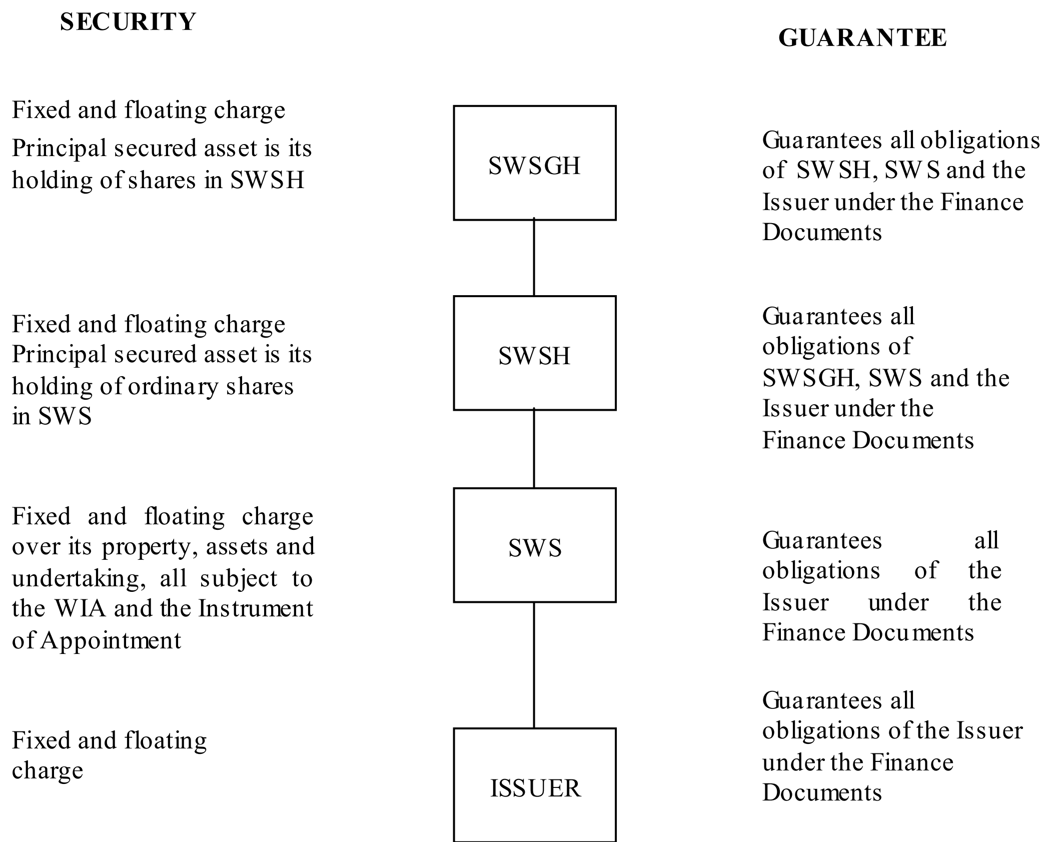
For a description of certain limitations on the ability of SWS to grant security and certain limitations and restrictions on the security purported to be granted, see Chapter 5 *"Risk Factors — Certain Legal Considerations — Security*" and Chapter 6 *"Water Regulation — Restrictions on the granting of security"*.

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

Neither SWSGH nor SWSH has any significant assets other than the shares in its respective subsidiary.

Security Structure

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



Financial Guarantor Documents

The Financial Guarantees of Wrapped Bonds

The form of Financial Guarantee, subject to completion and amendment, which is likely to be issued by MBIA (upon fulfilment or waiver by MBIA of certain conditions precedent contained in the CP Agreement) in respect of the issue of Class A Wrapped Bonds to be issued under the Programme is set out in full in Chapter 10 *"MBIA and its Financial Guarantees"* under *"MBIA's Financial Guarantee"*. To the extent that MBIA or any other Financial Guarantors issue Financial Guarantees in respect of any further Sub-Classes of Class A Wrapped Bonds and/or Class B Wrapped Bonds, such Financial Guarantees are expected to be issued by such Financial Guarantor(s) on terms substantially similar thereto.

Upon an early redemption of the relevant Class A Wrapped Bonds or an acceleration of the relevant Class A Wrapped Bonds. MBIA's obligations will continue to be to pay the Guaranteed Amounts as they fall Due for Payment (as defined in MBIA's Financial Guarantee) on each Payment Date. MBIA will not be obliged under any circumstances to accelerate payment under

its Financial Guarantees. However, if it does so, it may do so in its absolute discretion in whole or in part, and the amount payable by MBIA will be the outstanding principal amount (or pro rata amount that has become due and payable) of the relevant Class A Wrapped Bonds together with accrued interest (excluding always the FG Excepted Amounts). Any amounts due in excess of such outstanding principal amount (and any accrued interest thereon) will not be guaranteed by MBIA or any other Financial Guarantor under any of the Financial Guarantees.

The Bond Trustee will alone have the right to enforce the terms of Financial Guarantees issued in respect of Wrapped Bonds, and any right of any other person to do so is expressly excluded.

Guarantee and Reimbursement Deeds

On each relevant Issue Date, the Issuer and SWS will enter into a guarantee and reimbursement deed (each a "**G&R Deed**") with the relevant Financial Guarantor, pursuant to which the Issuer will be obliged, among other things, to reimburse such Financial Guarantor in respect of the payments made by it under the relevant Financial Guarantee and to pay, among other things, any financial guarantee fee and fees and expenses of such Financial Guarantor in respect of the provision of the relevant Financial Guarantee. Insofar as a Financial Guarantor makes payment under the relevant Financial Guarantee in respect of Guaranteed Amounts (as defined in such Financial Guarantee), it will be subrogated to the present and future rights of the relevant Wrapped Bondholders or relevant holders of other Wrapped Debt against the Issuer in respect of any payments made.

On the Initial Issue Date and on 27 May 2005, the Issuer and SWS entered into a G&R Deed with MBIA Assurance S.A. in respect of the Class A Wrapped Bonds issued on the Initial Issue Date and 27 May 2005, respectively.

Additional Resources Available

Initial Authorised Credit Facilities and the Second Artesian Term Facility

SWS entered into a facility agreement (the "**Initial RCF Agreement**") with an aggregate facility amount of £150,000,000 (the "**Initial RCF**") with RBS on the Initial Issue Date. The Initial RCF has now been syndicated. Under this facility agreement a £35,000,000 revolving credit facility is available to SWS for working capital requirements and a £115,000,000 revolving credit facility is available to SWS for capital expenditure requirements (in respect of capital expenditure which will qualify for an addition to RCV) from the Initial Issue Date until the final maturity date, being the business day before the fifth anniversary of the Initial Issue Date. The Initial RCF Agreement was amended and restated on 26 July 2005 to include Commerzbank AG, London Branch, HSBC Bank plc, ING Bank N.V., London Branch, and Sumitomo Mitsui Banking Corporation Europe Limited as additional lenders.

Drawings under the revolving credit facilities are subject to various conditions precedent as set out in the related facility agreement, including that no Event of Default or Potential Event of Default is subsisting, and in the case of a roll-over advance no Event of Default is subsisting, and each Repeating Representation is correct at the time of requesting and making the drawing. In the event of a Standstill, any outstanding Advances under the revolving credit facilities shall

convert into a term loan repayable on the earliest of (i) the termination of the Standstill; (ii) the final Maturity Date and (iii) the date of any acceleration under, and as permitted by, the STID.

Interest accrues on any drawing under the revolving credit facilities calculated at a daily rate by reference to applicable sterling LIBOR plus a margin and mandatory costs. SWS also pays certain agency, arrangement and underwriting fees and a commitment fee which accrues on any undrawn portion of the commitment under the revolving credit facilities.

The Issuer has also entered into a separate facility agreement with RBS under which RBS advanced to the Issuer a £165,000,000 index-linked term facility (the "**Initial Term Facility**"). RBS has transferred its rights and obligations in respect of the Initial Term Facility to Artesian Finance II plc ("**Artesian II**"). The advance under the Initial Term Facility has similar terms to Indexed Bonds in terms of interest accrual and payment, with a final repayment date in September 2033. The Issuer applied the proceeds of such advance in making an index-linked advance to SWS under the Initial Issuer/SWS Loan Agreement. Certain of the Issuer's payment obligations in respect of the advance under the Initial Term Facility are guaranteed by Financial Security Assurance (U.K.) Limited ("**FSA UK**")**,**a Financial Guarantor. The Issuer has given certain indemnities to Artesian II in connection with its funding of the Initial Term Facility.

The Initial RCF and the Initial Term Facility are referred to in this Prospectus as the **"Initial Authorised Credit Facilities".**

The Issuer has also entered into a separate facility agreement dated 5 July 2004 (the "**Second Artesian Term Facility Agreement**") with RBS under which RBS advanced to the Issuer a £156,484,023.05 index-linked term facility (the "**Second Artesian Term Facility**"). RBS has transferred its rights and obligations in respect of the Second Artesian Term Facility to Artesian Finance plc ("**Artesian**"). The advance under the Second Artesian Term Facility has similar terms to Indexed Bonds in terms of interest accrual and payment, with a final repayment date in September 2032. The Issuer applied the proceeds of such advance in making an index-linked advance to SWS under the Second Issuer/SWS Loan Agreement. Certain of the Issuer's payment obligations in respect of the advance under the Second Artesian Term Facility are guaranteed by FSA UK. The Issuer has given certain indemnities to Artesian in connection with its funding of the Second Artesian Term Facility.

SWS has entered into a revolving credit facility agreement (the "**Second Revolving Credit Facility**") with an aggregate facility amount of £120,000,000 arranged by RBS and Bayerische Landesbank, acting through its London Branch on 30 June 2005. The Second Revolving Credit Facility has not yet been drawn by SWS. Each loan under the Second Revolving Credit Facility may be used towards prepayment of the advances under the Third Issuer/SWS Loan Agreement or otherwise to meet the working capital expenditure requirements of SWS.

SWS and the Issuer make representations and warranties, covenants and undertakings to the Initial RCF Providers, Artesian II, Artesian, FSA UK and the Finance Parties party to the Second Revolving Credit Facility (the "**Second RCF Providers**") on the terms set out in the Common Terms Agreement. The Initial RCF Providers, Artesian II, Artesian and FSA UK and the Second RCF Providers have acceded to the STID and the CTA.

The Events of Default under the Common Terms Agreement apply under the Initial Authorised Credit Facilities, the Second Artesian Term Facility and the Second Revolving Credit Facility (see *"Common Terms Agreement"* above).

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

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

SWS and the Issuer have entered into loan insurance and indemnity agreements with FSA UK, under which: the Issuer agrees to reimburse to FSA UK amounts paid by FSA UK under FSA UK's guarantee of amounts payable by the Issuer under the Initial Term Facility and the Second Artesian Term Facility; the Issuer agrees to pay a fee to FSA UK and to pay, and to indemnify FSA UK against, certain other of FSA UK's costs and expenses; SWS and the Issuer made representations, warranties and covenants to FSA UK on the terms set out in the Common Terms Agreement; and SWS guarantees to FSA UK the Issuer's obligations to FSA UK under such agreements.

The Liquidity Facilities

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The DSR Liquidity Facility provided by The Royal Bank of Scotland plc and Barclays Bank plc (the "**Existing DSR Liquidity Facility Providers**") is the only Liquidity Facility in place as at the date of this Prospectus. The Issuer may establish further DSR Liquidity Facilities in connection with further Bonds and other Class A Debt and Class B Debt issued or incurred.

Under the terms of the Existing DSR Liquidity Facility Agreement, the Existing DSR Liquidity Facility Providers provide a 364 day commitment (which has been renewed) in an aggregate amount specified in the DSR Liquidity Facility Agreement to permit drawings to be made by the Issuer, in circumstances where there will be insufficient funds in the Debt Service Payment Account available on a Payment Date to pay amounts (other than principal amounts to be repaid in respect of Class A Debt and principal amounts to be repaid and any Subordinated Coupon Amounts to be paid in respect of Class B Debt or any termination payments under any Hedging Agreements) scheduled to be paid in respect of paragraphs (i) to (vi) inclusive and (ix) and, after deducting any prior ranking payments, (xii) of the Payment Priorities (a **"Liquidity Shortfall"**).

The Issuer will not be able to make a drawing in respect of a Liquidity Shortfall relating (in whole or in part) to Class B Debt unless the sum of the amount available under the DSR Liquidity Facilities and the amount standing to the credit of the Debt Service Reserve Account (immediately after such drawing) is not less than the next 12 months interest forecast on Class A Debt.

The Issuer may also enter into an O&M Reserve Facility Agreement with one or more Liquidity Facility Providers, drawings under which will be on-lent by the Issuer to SWS to meet SWS' operating and capital maintenance expenditure requirements to the extent that SWS has

insufficient funds available to it to meet these requirements. No O&M Reserve Facility Agreement has been entered into as at the date of this Prospectus.

Each Liquidity Facility Provider must be a bank which as at the relevant Issue Date has the Minimum Short-Term Rating (the "**Liquidity Facility Requisite Rating**").

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

Each Liquidity Facility Agreement does or will provide that amounts repaid by the Issuer may be redrawn.

Each Liquidity Facility Agreement does or will provide that if (i) at any time the rating of the relevant Liquidity Facility Provider falls below the Liquidity Facility Requisite Rating or (ii) the relevant Liquidity Facility Provider does not agree to renew its commitment under such Liquidity Facility prior to the expiry of the relevant availability period, the Issuer will:

(a) use all reasonable endeavours to replace the relevant Liquidity Facility Provider with a party having the Liquidity Facility Requisite Rating; and

(b) (if a replacement is not made within the relevant time period specified in the relevant Liquidity Facility Agreement) be entitled to require such Liquidity Facility Provider to pay into the Debt Service Reserve Account (in the case of a DSR Liquidity Facility) or the Issuer's O&M Reserve Account (in the case of an O&M Reserve Facility) the full amount of the relevant Liquidity Facility Provider's undrawn commitment (a **"Standby Drawing"**).

A Standby Drawing will generally be repayable only if the relevant Liquidity Facility Provider is re-rated with the Liquidity Facility Requisite Rating or confirmation is received from each of the Rating Agencies that either (i) the terms of a replacement Liquidity Facility or (ii) the absence of any such facility, in each case, as applicable, will not lead to a ratings downgrade of the Bonds from the relevant Rating Agencies.

Interest will accrue on any drawing (including a Standby Drawing) made under a Liquidity Facility provided by a Liquidity Facility Provider at a reference rate per annum plus a margin. Under the Liquidity Facility Agreements, the Issuer, in certain circumstances, will be required to pay additional amounts if: (i) a withholding or deduction for or on account of tax is imposed on payments made by it to the relevant Liquidity Facility Provider; or (ii) if the relevant Liquidity Facility Provider suffers an increase in the cost of providing the relevant Liquidity Facility. Drawings under any further Liquidity Facilities will accrue interest subject to the specific terms of the relevant Liquidity Facility Agreement. The Issuer will also pay certain agency, arrangement and renewal fees as well as a commitment fee which accrue on any undrawn portion of the commitments under the Liquidity Facilities.

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

Mezzanine Facility Agreements

The Issuer entered into (i) a senior mezzanine facility agreement with, amongst others, The Royal Bank of Scotland plc (as agent), RBEF Limited (as arranger), Royal Bank Investments Limited as the Original Senior Mezzanine Facility Provider and the Security Trustee in an aggregate amount of £127,200,000 (the "**Senior Mezzanine Facility Agreement**") and (ii) a junior mezzanine facility agreement with, amongst others, The Royal Bank of Scotland plc (as agent), RBEF Limited (as arranger), Royal Bank Investments Limited as original Junior Mezzanine Facility Provider and the Security Trustee, in an aggregate amount of £106,000,000 (the "**Junior Mezzanine Facility Agreement**" and, together with the Senior Mezzanine Facility Agreement, the "**Mezzanine Facility Agreements**"). The Mezzanine Facility Agreements have since been acquired by SWC. The Issuer borrowed the full amount available under the Mezzanine Facility Agreements on the Initial Issue Date and lent the proceeds thereof together with the nominal principal amount of the Bonds issued and borrowings under other Authorised Credit Facilities raised on the Initial Issue Date to SWS under the Initial Issuer/SWS Loan Agreement. SWS applied such loan proceeds, amongst other things, to repay its existing indebtedness to the Issuer and the Issuer applied such repayment proceeds to repay all of its indebtedness under the Bridge Facility Agreement and all of its indebtedness to SWI.

Interest accrues on any drawing under each Mezzanine Facility Agreement, in the case of the Senior Mezzanine Facility, at a floating rate of interest and, in the case of the Junior Mezzanine Facility, at a fixed rate. The Issuer's obligations to pay floating rate interest are hedged in accordance with the Hedging Agreements entered into on the Initial Issue Date (see *"Hedging Agreements"* below). The Issuer pays certain agency and arrangement fees under each Mezzanine Facility Agreement.

The Issuer has made representations and warranties, covenants and undertakings to the Mezzanine Facility Providers on the terms set out in the Common Terms Agreement. The Events of Default under the Common Terms Agreement apply under the Mezzanine Facility Agreements (see *"Common Terms Agreement"* above).

The Issuer's payment obligations are backed by advances owing to the Issuer pursuant to the Initial Issuer/SWS Loan Agreement and the terms of those advances in terms of amounts, interest rates, tenor and payment dates correspond with the relevant advances under the Mezzanine Facility Agreements (or in the case of the Senior Mezzanine Facility, the related Interest Rate Hedging Agreements).

Under the terms of the CTA, neither SWS nor the Issuer is allowed to make any payments of interest, principal or any other amounts under the Mezzanine Facility Agreements or the corresponding advances under the Initial Issuer/SWS Loan Agreement (save for mandatory prepayments in the event of, amongst other things, illegality) unless the Restricted Payment Condition is satisfied or pursuant to a Subordinated Debt Replacement Event.

The claims of the Mezzanine Facility Providers are secured under the terms of the Security Documents but are subordinated to the Class A Debt and the Class B Debt in accordance with the Payment Priorities. In the event of any failure to meet the Restricted Payment Condition on any payment date or if, following satisfaction of the Restricted Payment Condition, there is a

shortfall in cash available to pay amounts due and payable under the Mezzanine Facility Agreements, the amount of the shortfall will not be treated as due and instead shall be deferred until the payment date on which the Issuer has sufficient funds to meet such payment or the final maturity date of any outstanding senior debt. The ability of the Mezzanine Facility Providers to accelerate any sums owing to them under the Mezzanine Facility Agreements upon or following the occurrence of an Event of Default is postponed to the rights of the holders of Class A Debt and the Class B Debt pursuant to the STID.

The Mezzanine Facility Providers are subject to certain call option arrangements in relation to their Mezzanine Debt which may be exercised against them following enforcement of any of the security granted by SWSGH and/or SWSH (see *"Security Trust and Intercreditor Deed — Enforcement"* above).

SWS Preference Shares

SWS has issued (i) fixed dividend (£40 per share net) cumulative redeemable preference shares 2038 of £1 each in the capital of SWS (the "**Class A1 Preference Shares**"), (ii) non-voting participating cumulative redeemable preference shares 2038 of 1p each in the capital of SWS (the **"Class A2 Preference Shares")** and (iii) fixed dividend (£70 per share net) cumulative redeemable preference shares 2038 of £1 each in the capital of SWS **(**the "**Class B Preference Shares**" and together with the Class A1 Preference Shares and Class A2 Preference Shares the "**SWS Preference Shares**"). The SWS Preference Shares are non-voting save in respect of certain limited matters which are specific to the rights and value of the SWS Preference Shares.

Under the terms of the CTA, SWS is not allowed to make any payments on or under the SWS Preference Shares unless the Restricted Payment Condition is satisfied (see *"Common Terms Agreement"* above).

The holders of the SWS Preference Shares enjoy certain specific and protective entrenched rights. These can be waived in accordance with the terms and conditions of the SWS Preference Shares and in addition, and amongst other things, will have no effect, and will not require SWS to obtain any consent or sanction of the SWS Preference Shareholders unless the proposed event or action would or could reasonably be expected to have a material adverse effect on the fundamental terms or value of their investment. For example, for so long as neither an Event of Default is continuing nor, if a Trigger Event has occurred and is continuing, has a Remedial Plan concluded that the failure to raise new Financial Indebtedness in the circumstances described below would lead to an Event of Default, in the circumstance where the Mezzanine Facility Providers would have an equivalent Entrenched Right (as described earlier in *"Security Trust and Intercreditor Deed — Entrenched Rights of the Mezzanine Facility Providers")*, the articles of association of SWS provide that SWS may not agree any modification to, or consent or waiver under or in respect of, any term of any Finance Document if the proposed modification, consent or waiver would permit the raising of new Financial Indebtedness by the SWS Financing Group to the extent that, as a result, the aggregate of the Senior Net Indebtedness and any other net indebtedness ranking in point of priority senior to the Senior Mezzanine Debt would exceed 90 percent. of RCV, unless the Security Trustee has received consent from the holders of more than 50 per cent. of the aggregate nominal value of all classes of SWS Preference Shareholders or the sanction of an ordinary resolution passed at a separate general meeting of the holders of all

classes of the SWS Preference Shares. Certain of these other key rights are also disapplied following an Event of Default.

The SWS Preference Shares may in certain circumstances be converted into Subordinated Debt of SWS, whereupon the holders of such Subordinated Debt will be required either to accede to the STID and the CTA for the purposes of, *inter alia*, taking the benefit of the Security and subordinating their secured claims to those of the holders of Class A Debt, the Class B Debt and the Mezzanine Debt or to accede to the SWS Preference Share Deed (as defined below) for the purpose of, *inter alia*, restricting their right to accelerate their unsecured claims during a Standstill Period.

The initial holders of the SWS Preference Shares entered into a deed on the Initial Issue Date with the Security Trustee and the Obligors (the "**SWS Preference Share Deed**") pursuant to which SWS agreed not to, and such holders of the SWS Preference Shares agreed not to permit or require SWS to, make any Distribution in respect of the SWS Preference Shares unless the Restricted Payment Condition is satisfied at such time and payments made in breach of the Restricted Payment Condition shall be immediately repaid to the Security Trustee and pending such repayment shall be held on trust for the Security Trustee. Under call option arrangements contained in the SWS Preference Share Deed, each holder of the SWS Preference Shares (other than the Class A2 Preference Shares) will be required to sell its SWS Preference Shares to any person who acquires the ordinary shares in SWSH or SWS following an enforcement of the Security granted by SWSGH or SWSH (or to any nominee of such person) for a consideration calculated to ensure that the price that such holder of the SWS Preference Shares receives will not be less than the price it would have received for its holding had its SWS Preference Shares been charged in favour of the Security Trustee as security for Secured Liabilities and sold as part of any disposal of the Security Assets on an enforcement of the Security granted by SWSGH and/or SWSH. In this event, the rights of the holders of the Class A2 Preference Shares will be deferred.

SWC owns the Class A1 Preference Shares and the Class B Preference Shares. SWI owns the Class A2 Preference Shares. Each of SWC and SWI has acceded to the SWS Preference Share Deed.

Hedging Agreements

Hedging Policy

The Hedging Policy provides that the SWS Financing Group must enter into Hedging Agreements in accordance with the Hedging Policy and that the only member of the SWS Financing Group that may enter into Hedging Agreements is the Issuer, provided that the Issuer may enter into back-to-back swap arrangements with SWS in respect of Hedging Agreements entered into by the Issuer to hedge the obligations of SWS under Finance Leases or any other Authorised Credit Facility raised by SWS or which are otherwise not directly linked to the raising of new debt under an Authorised Credit Facility.

However, STID Proposals have been granted allowing SWS to enter into Hedging Agreements in connection with the Second Revolving Credit Facility.

The Hedging Policy provides, *inter alia*, that:

1. The SWS Financing Group will not enter into Treasury Transactions for the purpose of speculation, but rather only to manage risk inherent in its business or funding on a prudent basis.

2. Any change to the Hedging Policy will be subject to SWS board approval and may only be made with the approval of the Security Trustee (such approval not to be unreasonably withheld).

3. Subject to such approvals, the Hedging Policy will be reviewed from time to time by the SWS Financing Group and amended (subject to Entrenched Rights and Reserved Matters and in accordance with the provisions of the STID) as appropriate in line with market developments, regulatory developments, and Good Industry Practice.

4. The SWS Financing Group must not bear currency risk in respect of any foreign currency denominated debt instruments, or in respect of any significant foreign currency purchases.

5. The SWS Financing Group must hedge its exposure to interest rate risk on at least 85 per cent. of its total outstanding debt liabilities for the current period to the next Periodic Review and at least 70 per cent. in the next period to the subsequent Periodic Review (each to be adjusted to the extent that the period from one Periodic Review to the next Periodic Review is greater than five years) (on a rolling basis). This figure will be kept under review with respect to market conditions and developments in regulatory methodology and practice.

6. Interest rate risk on floating rate liabilities may be hedged through a combination of cash balances. Authorised Investments and instruments such as interest rate swaps entered into by the Issuer.

7. The SWS Financing Group may manage its exposure to inflation risk through the use of index-linked instruments where it is cost effective.

8. The Issuer may only enter into Treasury Transactions with counterparties whose short-term, unsecured and unsubordinated debt obligations are assigned a rating by the Rating Agencies which is no less than the Minimum Short-term Rating and whose long-term, unsecured and unsubordinated debt obligations are assigned a rating by Moody’s of at least A2 (the “**Moody’s Minimum Long-term Rating**”), or where a parent guarantee is provided by an institution which meets the same criteria. Each Hedging Agreement is to include a provision entitling the Issuer to terminate if there is a Hedge Counterparty Downgrade as described below.

9. Hedging Agreements must be entered into in the form, as amended by the parties thereto, of the 1992 ISDA Master Agreement (Multicurrency — Cross Border), the 2002 Master Agreement published by ISDA or any successor thereto published by ISDA unless otherwise agreed by the Security Trustee.

Hedging Agreements

The Existing Hedging Agreements

The Issuer has entered into various interest rate and currency swap transactions with the Initial Hedge Counterparties (the "**Existing Hedging Agreements**") in conformity with the Hedging Policy.

SWS Hedging Agreements

SWS has entered into various interest rate swap transactions with RBS and Citibank N.A., London Branch in connection with the Second Revolving Credit Facility (the "**SWS Hedging Agreements**").

Tax

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

Termination

The Issuer (or, in the case of the SWS Hedging Agreements, SWS) will be entitled to terminate a Hedging Agreement in certain circumstances (including a failure to pay by the Hedge Counterparty, certain insolvency events affecting the Hedge Counterparty and certain rating downgrade events affecting the Hedge Counterparty).

The Hedge Counterparty will be entitled to terminate a Hedging Agreement only in certain limited circumstances being:

- a failure by the Issuer (or, in the case of the SWS Hedging Agreements, SWS) to make payment when due;
- certain insolvency events affecting the Issuer (or, in the case of the SWS Hedging Agreements, SWS);
- illegality affecting the Hedging Agreement;

- certain tax events (including as described above);
- redemption in whole or in part of any Sub-Class of the Bonds hedged by such Treasury Transaction;
- termination of a Standstill Period (except by virtue of remedy, revocation or waiver of the relevant Event of Default giving rise to the Standstill Period) or, if earlier, an Acceleration of any Sub-Class of the Bonds hedged by such Treasury Transaction pursuant to Condition 11 of the Bonds; and
- (subject to the provisions described below) upon the exercise of an option to terminate a Hedging Agreement on the tenth anniversary of the effective date of the relevant Hedging Transaction or at five yearly intervals thereafter.

The Issuer may enter into Treasury Transactions with Hedge Counterparties pursuant to which each relevant Hedge Counterparty has the right to terminate the relevant Treasury Transaction on the tenth anniversary of the effective date of such Treasury Transaction and thereafter no more frequently than at five-yearly intervals provided that (a) the relevant Hedge Counterparty gives the Issuer at least one year's prior notice in writing of its intention to exercise such right of termination; and (b) the aggregate notional amount and/or sterling currency amounts (as applicable) of Treasury Transactions pursuant to which Hedge Counterparties have such right of termination does not exceed 10 per cent. of RCV.

Within three months of the receipt of a notice of termination from the relevant Hedge Counterparty, the Issuer shall use all reasonable endeavours to enter into new Treasury Transaction(s) in order to replace the Treasury Transaction which is the subject of such notice of termination.

In the event that a Hedging Agreement or a Treasury Transaction is terminated, a termination payment may be due from the Issuer.

Hedge Counterparty Rating Downgrade

If a Hedge Counterparty falls below the Minimum Short-term Rating or the Moody's Minimum Long-term Rating (a "**Hedge Counterparty Downgrade**") and as a result of such Hedge Counterparty Downgrade the then current rating of the Class A Unwrapped Bonds (or, if no Class A Unwrapped Bonds are outstanding, the then current shadow rating of the Class A Wrapped Bonds or, if there are no Class A Bonds outstanding, the then current rating of the Class B Unwrapped Bonds, or if there are no Class A Bonds or Class B Unwrapped Bonds outstanding, the then current shadow rating of the Class B Wrapped Bonds) would be downgraded or placed under review for possible downgrade by any of the Rating Agencies (a "**Bond Downgrade**") and the Hedge Counterparty has not, within 30 days of being notified of such Bond Downgrade, at its own cost either:

(a) procured that its obligations with respect to the relevant Hedging Agreement are guaranteed by a third party which has a rating of no less than the relevant Minimum Short-term Rating and the Moody's Minimum Long-term Rating; or

(b) put in place an appropriate mark-to-market collateral agreement in accordance with the requirements specified in the relevant Hedging Agreement in support of its obligations under the relevant Hedging Agreement; or

(c) transferred all of its rights and obligations under the Hedging Agreement to a replacement third party which is rated no less than the Minimum Short-term Rating and the Moody's Minimum Long-term Rating; or

(d) taken such other action as the Hedge Counterparty agrees which will result in the rating (or shadow rating, as applicable) of the relevant Bonds being restored to the level they were immediately prior to the Hedge Counterparty Downgrade,

then the Issuer shall be entitled to terminate the relevant Hedging Agreement.

Other Transaction Documents

Account Bank Agreement

Pursuant to the Account Bank Agreement, the Account Bank has agreed to hold the Accounts and operate them in accordance with the instructions of the Cash Manager or Standstill Cash Manager (as applicable). The Cash Manager or Standstill Cash Manager (as applicable) will manage the Accounts on behalf of the SWS Financing Group pursuant to the Common Terms Agreement (see *"Cash Management"* above).

Registered Office Agreement

Pursuant to a registered office agreement entered into between the Issuer and M&C Corporate Services Limited on 1 January 2002 (the "**Registered Office Agreement**"), M&C Corporate Services Limited and/or Maples and Calder provide certain corporate services to the Issuer.

Tax Deeds of Covenant

SW Tax Deed of Covenant

Under the terms of the SW Tax Deed of Covenant, each Obligor has given certain representations and covenants as to its tax status and to the effect that, subject to SWS' membership of the SWS VAT Group, it has not taken and, save in certain permitted circumstances, will not take any steps which might reasonably be expected to give rise to a liability to tax for an Obligor where that tax is primarily the liability of another person. Certain other companies including SWC and SWI have also represented and covenanted that they have not taken nor will take any steps which might reasonably be expected to give rise to a liability for tax for an Obligor where that tax is primarily the liability of another person.

With a view to preventing a liability to tax arising for an Obligor which is primarily the liability of another person, SWI (among others) will, under the SW Tax Deed of Covenant, incur certain obligations in relation to specified events and any change in tax residence of the Obligors. For example, the SW Tax Deed of Covenant provides that in certain circumstances where it is anticipated that there will be a change of control for tax purposes of SWSGH and therefore of the

Obligors (say, as a result of the sale of shares in SWC or SWI), SWI can be required, as a condition of that sale, to deposit an amount in a trust account equal to the estimated tax liability (if any) arising or likely to arise in an Obligor as a result of the sale. The money deposited could then be used to pay the tax liability of the Obligor.

Shareholder Tax Deed of Covenant

Under the terms of the Shareholder Tax Deed of Covenant, each of Veolia Environnement S.A. (which was then an indirect shareholder of SWS) and RBSG, covenanted to the Security Trustee that it and the companies which are controlled by it for tax purposes (excluding in the case of RBSG, SWC, SWI and their Subsidiaries) have not taken and will not take any steps which might reasonably be expected to give rise to a liability to tax for the Obligors where that tax is primarily the liability of a company controlled by it (excluding in the case of RBSG, SWC, SWI and their Subsidiaries).

RBSG has also covenanted to the Security Trustee to procure that an equivalent covenant is given by any person (and its ultimate parent) which obtains control of SWSGH in certain circumstances.

SWS/SWSG Loan Agreement

SWSG is indebted to SWS in the principal amount of approximately £800,000,000 (the "**SWS/SWSG Loan**"). The terms of the SWS/SWSG Loan are set out in a loan agreement entered into between SWS and SWSG on the Initial Issue Date (the "**SWS/SWSG Loan Agreement**"). Interest accrues on the SWS/SWSG Loan at the rate of 7 per cent. per annum payable quarterly to the extent that SWSG has on such interest payment date received on such date a dividend from SWS (through SWSH and SWSGH) and/or a payment from SWS for a Permitted Tax Loss Transaction, in each case paid by SWS solely for the purpose of enabling SWSG to meet its scheduled payment obligations under the SWS/SWSG Loan (such dividend payment or payment for a Permitted Tax Loss Transaction a "**SWS/SWSG Debt Service Distribution**"). Interest will roll-up to the extent that SWSG is not put in funds to meet its scheduled payment obligations and the unpaid amount will itself accrue interest at the relevant interest rate.

The SWS/SWSG Loan is secured by a full first ranking debenture granted by SWSG in favour of SWS on the Initial Issue Date creating, *inter alia,* a first fixed charge over SWSG's shares in SWSGH and related rights, a first fixed charge over SWSG's bank account with the Account Bank into which any SWS/SWSG Debt Service Distribution to it is paid and a first floating charge over all of SWSG's assets, revenues and undertakings. The security will not operate as a fetter on SWSG's ability to dispose of the shares in SWSGH provided that the proceeds from such disposal are sufficient to enable SWSG to repay all amounts outstanding under the SWS/SWSG Loan Agreement.

No SWS/SWSG Debt Service Distribution may be made unless, among other things (a) in the case of a dividend payment, the dividend has been validly declared; (b) in the case of a payment for Permitted Tax Loss Transaction, the payment when made complies in all respects with the SW Tax Deed of Covenant and the CTA; (c) each payment is made against irrevocable payment

instructions from SWSG directing the Account Bank to remit the proceeds of such payment on receipt by SWSG directly to an Operating Account of SWS for same day value; (d) no Event of Default is subsisting or would result from the payment; and (e) no event of default under the SWS/SWSG Loan Agreement has occurred and is continuing.

An event of default under the SWS/SWSG Loan Agreement will occur and the security granted by SWSG will become immediately enforceable if SWSG defaults on any of its payment obligations to pay interest or principal, breaches any warranty or covenant contained in the SWS/SWSG Loan Agreement or SWSG commits a TDC Breach (as defined in the SW Tax Deed of Covenant) which has a material adverse effect, becomes insolvent or if the security granted by SWSG becomes invalid.

CHAPTER 8
THE BONDS

Terms and Conditions of the Bonds

The following is the text of the terms and conditions which (subject to completion and amendment and as supplemented or varied in accordance with the provisions of the relevant Final Terms (as defined below) and, save for the italicised paragraphs) will be incorporated by reference into each Global Bond (as defined below) representing Bonds (as defined below) in bearer form, Bonds in definitive form (if any) issued in exchange for the Global Bond(s) representing Bonds in bearer form, each Global Bond Certificate (as defined below) representing Bonds in registered form and each Individual Bond Certificate (as defined below) representing Bonds in registered form (only if such incorporation by reference is permitted by the rules of the relevant stock exchange and agreed by the Issuer). If such incorporation by reference is not so permitted and agreed, each Bond in bearer form and each Individual Bond Certificate representing Bonds in registered form will have endorsed thereon or attached thereto such text (as so completed, amended, varied or supplemented). Further information with respect to each Tranche (as defined below) of Bonds will be given in the relevant Final Terms which will provide for those aspects of these Conditions which are applicable to such Tranche (as defined below) of Bonds, including, in the case of Wrapped Bonds (as defined below), the form of Financial Guarantee (as defined below) and endorsement and, in the case of all Sub-Classes (as defined below), the terms of the relevant advance under the relevant Issuer/SWS Loan Agreement. If a Financial Guarantor (as defined below) other than MBIA (as defined below) is appointed in relation to any Sub-Class of Wrapped Bonds (as specified in the relevant Final Terms) a supplement to this Prospectus will be produced providing such information about such Financial Guarantor as may be required by the rules of the UK Listing Authority, the London Stock Exchange or such other listing authority or stock exchange on which such Bonds are admitted to listing and/or trading. References in the Conditions to "Bonds" are. as the context requires, references to the Bonds of one Sub-Class only, not to all Bonds which may be issued under the Programme.

Southern Water Services (Finance) Limited (the "**Issuer**") has established a guaranteed bond programme (the "**Programme**") for the issuance of up to £6,000,000,000 guaranteed bonds (the "**Bonds**"). Bonds issued under the Programme on a particular Issue Date comprise a Series (a "**Series**"), and each Series comprises one or more Classes of Bonds (each a "**Class**"). Each Class may comprise one or more sub-classes (each a "**Sub-Class**") and each Sub-Class comprising one or more tranche (each a "**Tranche**").

The guaranteed wrapped bonds will be designated as "**Class A Wrapped Bonds**" or "**Class B Wrapped Bonds**". The guaranteed unwrapped bonds will be designated as "**Class A Unwrapped Bonds**" (and together with the "**Class A Wrapped Bonds**", the "**Class A Bonds**") or "**Class B Unwrapped Bonds**" (and together with the "**Class B Wrapped Bonds**", the "**Class B Bonds**"). Each Sub-Class will be denominated in different currencies or having different interest rates, maturity dates or other terms. Bonds

of any Class may be zero coupon ("**Zero Coupon Bonds**"), fixed rate ("**Fixed Rate Bonds**"), floating rate ("**Floating Rate Bonds**"), index-linked ("**Indexed Bonds**"), dual currency bonds ("**Dual Currency Bonds**"), partly paid bonds ("**Partly Paid Bonds**") or instalment bonds ("**Instalment Bonds**") depending on the method of calculating interest payable in respect of such Bonds and may be denominated in sterling, euro, U.S. dollars or in other currencies subject to compliance with applicable law.

The terms and conditions applicable to any particular Sub-Class of Bonds are these terms and conditions ("**Conditions**") as supplemented, amended and/or replaced by a set of final terms in relation to such Sub-Class ("**Final Terms**"). In the event of any inconsistency between these Conditions and the relevant Final Terms, the relevant Final Terms shall prevail.

The Final Terms for this Bond (or the relevant provisions thereof) supplement these Conditions and may specify other terms and conditions which shall, to the extent so specified or to the extent inconsistent with these Conditions, replace or modify these Conditions for the purposes of this Bond. Reference to the "**Final Terms**" is to the Final Terms (or the relevant provisions thereof) applicable to this Bond.

The Bonds are subject to and have the benefit of a trust deed dated the Initial Issue Date (as defined below) (as amended by a Deed of Amendment dated 20 May 2005 and as further amended by a Second Deed of Amendment dated 13 October 2006 and as further amended, supplemented, restated and/or novated from time to time, the "**Bond Trust Deed**") between the Issuer, MBIA Assurance S.A. or another Financial Guarantor (as defined below) acceding thereto and Deutsche Trustee Company Limited as trustee (the "**Bond Trustee**", which expression includes the trustee or trustees for the time being of the Bond Trust Deed).

The Class A Wrapped Bonds and the Class B Wrapped Bonds (each "**Wrapped Bonds**") alone will be unconditionally and irrevocably guaranteed as to scheduled payments of principal and interest (as adjusted for indexation, as applicable, but excluding any additional amounts relating to premium, prepayment or acceleration, accelerated amounts and amounts (if any) by which, in the case of Fixed Rate Bonds or Indexed Bonds (other than deferred interest), the Coupons (as defined below) exceeds the initial Coupons on such Sub-Class as at the relevant Issue Date (as defined in Condition 6(i) *(Definitions)),* and, in the case of Floating Rate Bonds, the Margin on the Coupons (as defined below) exceeds the initial Margin on the Coupons on such Sub-Class as at the relevant Issue Date (as defined in Condition 6(i) *(Definitions))* (in each case, the "**Subordinated Coupon Amounts**"), all such amounts being the "**FG Excepted Amounts**") pursuant to a financial guarantee (each, a "**Financial Guarantee**") to be issued by MBIA UK Insurance Limited ("**MBIA**") or another financial guarantor (MBIA and each other such financial guarantor being a "**Financial Guarantor**") in conjunction with the issue of each Sub-Class of Bonds.

Neither of the Class A Unwrapped Bonds or the Class B Unwrapped Bonds (each "**Unwrapped Bonds**") will have the benefit of any such Financial Guarantee.

The Bonds have the benefit (to the extent applicable) of an agency agreement (as amended, supplemented and/or restated from time to time, the "**Agency Agreement**") dated the Initial Issue Date (to which the Issuer, the Bond Trustee, the Principal Paying Agent and the other Paying Agents (in the case of Bearer Bonds) or the Transfer Agents and the Registrar (in the case of Registered Bonds) are party). As used herein, each of "**Principal Paying Agent**", "**Paying Agents**", "**Agent Bank**", "**Transfer Agents**" and/or "**Registrar**" means, in relation to the Bonds, the persons specified in the Agency Agreement as the Principal Paying Agent, Paying Agents, Agent Bank, Transfer Agents and/or Registrar, respectively, and, in each case, any successor to such person in such capacity. The Bonds may also have the benefit (to the extent applicable) of a calculation agency agreement (in the form or substantially in the form of Schedule 1 to the Agency Agreement, the "**Calculation Agency Agreement**") between, *inter alia*, the Issuer and any calculation agent appointed by the Issuer as calculation agent (the "**Calculation Agent**").

On 23 July 2003 (the "**Initial Issue Date**"), the Issuer entered into a security agreement (the "**Security Agreement**") with Deutsche Trustee Company Limited as security trustee (the "**Security Trustee**"), pursuant to which the Issuer granted certain fixed and floating charge security (the "**Issuer Security**") to the Security Trustee for itself and on behalf of the other Secured Creditors (as defined below), the Bond Trustee (for itself and on behalf of the Bondholders), the Bondholders, each Financial Guarantor, the Issuer, each Liquidity Facility Provider, the Hedge Counterparties, the Initial Authorised Credit Facility Arranger, the Liquidity Facility Agents, the Initial Authorised Credit Facility Agent, the Initial Authorised Credit Provider and each Authorised Credit Provider (as defined below), each Agent, the Cash Manager (other than when the Cash Manager is SWS), the Standstill Cash Manager, any Additional Secured Creditors (each as defined therein) and the Mezzanine Finance Parties (together, the "**Secured Creditors**"). On the Initial Issue Date, the Issuer entered into a security trust and intercreditor deed (the "**STID**") with, among others, the Security Trustee and other Secured Creditors and pursuant to which the Security Trustee holds the Security on trust for the Secured Creditors and the Secured Creditors agree to certain intercreditor arrangements.

On or about the date of this Prospectus, the Issuer entered into an amended and restated Dealership Agreement (the "**Dealership Agreement**") with the dealers named therein (the "**Dealers**") in respect of the Programme, pursuant to which any of the Dealers may enter into a subscription agreement in relation to each Sub-Class of Bonds issued by the Issuer, and pursuant to which the Dealers have agreed to subscribe for the relevant Sub-Class of Bonds on behalf of the Issuer. In any subscriptions agreement relating to a Sub-Class of Bonds, any of the Dealers may agree to procure subscribers to subscribe for the relevant Sub-Class of Bonds.

On the Initial Issue Date, the Issuer entered into a common terms agreement (the "**Common Terms Agreement**") with, among others, the Security Trustee, pursuant to which the Issuer makes certain representations, warranties and covenants and which sets out in Schedule 7 thereof the Events of Default (as defined therein) in relation to the Bonds.

The Issuer has entered or may enter into liquidity facility agreements (together, the "**Liquidity Facility Agreements**") with certain liquidity facility providers (together, the "**Liquidity Facility Providers**") pursuant to which the Liquidity Facility Providers agree to make certain facilities available to meet liqu4idity shortfalls (including debt service liquidity shortfalls and shortfalls in operating and maintenance expenditure of SWS).

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

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

The Bond Trust Deed, the Bonds (including the applicable Final Terms), the Security Agreement, the STID (the STID, the Security Agreement and any other documentation evidencing or creating security over any asset of an Obligor to a Secured Creditor under the Finance Documents being together the "**Security Documents**"), the Financial Guarantee Fee Letters, the Finance Lease Documents, the Agency Agreement, the Liquidity Facility Agreements, the Hedging Agreements, the Initial Term Facility Agreement, the Initial RCF Agreement, the Second Artesian Term Facility Agreement, the Issuer/SWS Loan Agreements, the G&R Deeds, the Financial Guarantees, the Common Terms Agreement, the Mezzanine Facility Agreements, the CP Agreement, any other Authorised Credit Facilities, the master definitions agreement between, among others, the Issuer and the Security Trustee dated the Initial Issue Date (as amended, supplemented and/or restated from time to time, the "**Master Definitions Agreement**"), the account bank agreement between, among others, the account bank, the Issuer and the Security Trustee (the "**Account Bank Agreement**"), the Tax Deeds of Covenant and the indemnification deed between, among others, the Financial Guarantor(s) and the Dealers dated 18 July 2003 (the "**Indemnification Deed**"), the SWS Preference Share Deed, the SWS/SWSG Loan Agreement and any related security document (each, if not defined above, as defined below or in the Master Definitions Agreement) are, in relation to the Bonds, (and together with each other agreement or instrument between SWS or the Issuer (as applicable) and an Additional Secured Creditor designated as a Finance Document by SWS or the Issuer (as applicable), the Security Trustee and such Additional Secured Creditor in the Accession Memorandum of such Additional Secured Creditor) together referred to as the "**Finance Documents**".

Terms not defined in these Conditions have the meaning set out in the Master Definitions Agreement.

Certain statements in these Conditions are summaries of the detailed provisions appearing on the face of the Bonds (which expression shall include the body thereof), in

the relevant Final Terms or in the Bond Trust Deed, the Security Agreement or the STID. Copies of, *inter alia,* the Finance Documents are available for inspection during normal business hours at the specified offices of the Principal Paying Agent (in the case of bearer Bonds) or the specified offices of the Transfer Agents and the Registrar (in the case of registered Bonds), save that, if this Bond is an unlisted Bond of any Sub-Class, the applicable Final Terms will only be obtainable by a Bondholder holding one or more unlisted Bonds of that Sub-Class and such Bondholder must provide evidence satisfactory to the Issuer and the relevant Agent as to its holding of such Bonds and identity.

The Bondholders (as defined below) are entitled to the benefit of, are bound by, and are deemed to have notice of, all the provisions of the Bond Trust Deed, the STID, the Security Agreement, the Common Terms Agreement and the relevant Final Terms and to have notice of those provisions of the Agency Agreement and the other Finance Documents applicable to them.

Any reference in these conditions to a matter being "**specified**" means as the same may specified in the relevant Final Terms.

1 Form, Denomination and Title

(a) Form and Denomination

The Bonds are in bearer form ("**Bearer Bonds**") or in registered form ("**Registered Bonds**") as specified in the applicable Final Terms and, serially numbered in the Specified Denomination(s) provided that in the case of any Bonds which are to be admitted to trading on a regulated market within the European Economic Area or offered to the public in a Member State of the European Economic Area in circumstances which require the publication of a prospectus under the Prospectus Directive, the minimum Specified Denomination shall be €50,000 (or its equivalent in any other currency as at the date of issue of the relevant Bonds). Bonds of one Specified Denomination may not be exchanged for Bonds of another Specified Denomination and Bearer Bonds may not be exchanged for Registered Bonds and *vice versa*. References in these Conditions to "**Bonds**" include Bearer Bonds and Registered Bonds and all Sub-Classes, classes, Tranches and Series.

So long as the Bonds are represented by a temporary Global Bond or permanent Global Bond and the relevant clearing system(s) so permit, the Bonds shall be tradeable only in principal amounts of at least the Specified Denomination (or if more than one Specified Denomination, the lowest Specified Denomination) provided hereon and integral multiples of the Tradeable Amount (as defined in the relevant Final Terms) provided in the relevant Final Terms.

Interest-bearing Bearer Bonds are issued with Coupons (as defined below) (and, where appropriate, a Talon, (as defined below)) attached. After all the Coupons attached to, or issued in respect of, any Bearer Bond which was issued with a

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

(b) *Title*

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

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

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

Bonds which are represented by a Global Bond or Global Bond Certificate will be transferable only in accordance with the rules and procedures for the time being of Euroclear and Clearstream, Luxembourg, as the case may be. References to Euroclear and/or Clearstream, Luxembourg shall, whenever the context so permits, be deemed to include a reference to any additional or alternative clearing system specified in the applicable Final Terms or as may otherwise be approved by the Issuer, the Principal Paying Agent and the Bond Trustee.

(c) *Fungible Issues of Bonds comprising a Sub-Class*

A Sub-Class of Bonds may comprise a number of issues in addition to the initial Tranche of such Sub-Class, each of which will be issued on identical terms save for the first interest payment, the Issue Date and the Issue Price. Such further issues of the same Sub-Class will be consolidated and form a Series with the prior issues of that Sub-Class.

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

(a) *Exchange of Bonds*

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

Registered Bonds may not be exchanged for Bearer Bonds.

(b) *Transfer of Registered Bonds*

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

(c) Delivery of New Individual Bond Certificates

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

(d) Exchange at the Expense of Transferor Bondholder

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

(e) Closed Periods

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

3 Status of Bonds and Financial Guarantee

(a) Status of Class A Bonds

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

The Class A Bonds, Class A Coupons, Class A Talons and Class A Receipts (if any) are direct and unconditional obligations of the Issuer, are secured in the manner described in Condition 4 *(Security, Priority and Relationship with Secured Creditors*) and rank *pari passu* without any preference among themselves. However, the Class A Unwrapped Bonds will not have the benefit of any Financial Guarantee.

(b) Status of Class B Bonds

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

The Class B Bonds, Class B Coupons, Class B Talons and Class B Receipts (if any) are direct and unconditional obligations of the Issuer, are secured in the manner described in Condition 4 *(Security, Priority and Relationship with Secured Creditors)*, are subordinated to the Class A Bonds, Class A Coupons, Class A Receipts and Class A Talons (if any) and rank *pari passu* without any preference among themselves. However, the Class B Unwrapped Bonds will not have the benefit of any Financial Guarantee.

(c) *Financial Guarantee Issued by Financial Guarantor*

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

Each Sub-Class of each Class of Wrapped Bonds will have the benefit of a Financial Guarantee issued by a Financial Guarantor, issued pursuant to a guarantee and reimbursement deed between, amongst others, the Issuer and a Financial Guarantor dated on or before the relevant Issue Date (as defined below) of such Bonds (each a "**G&R Deed**"). Under the relevant Financial Guarantee, the relevant Financial Guarantor unconditionally and irrevocably agrees to pay to the Bond Trustee all sums due and payable but unpaid by the Issuer in respect of scheduled interest and payment of principal (but excluding FG Excepted Amounts) on such Wrapped Bonds, all as more particularly described in the relevant Financial Guarantee.

The terms of the relevant Financial Guarantee provide that amounts of principal on any such Bonds which have become immediately due and payable (whether by virtue of acceleration, prepayment or otherwise) other than on the relevant Payment Date (as defined under the Financial Guarantee) will not be treated as Guaranteed Amounts (as defined in the Financial Guarantee) which are Due for Payment (as defined in the Financial Guarantee) under the Financial Guarantee unless the Financial Guarantor in its sole discretion elects so to do by notice in writing to the Bond Trustee. The Financial Guarantor may elect to accelerate payments due under the Financial Guarantee in full or partially. All payments made by the relevant Financial Guarantor under the relevant Financial Guarantee in respect of partial acceleration shall be applied (i) to pay the Interest (as defined in the relevant Financial Guarantee) accrued but unpaid on the Principal (as defined in the relevant Financial Guarantee) of such part of the accelerated payment and (ii) to reduce the Principal (as defined in the relevant Financial Guarantee) (or, in the case of Wrapped Bonds repayable in instalments, each principal repayment instalment on a pro rata basis with a corresponding reduction of each amount of the Interest (as determined in the Financial Guarantee)) outstanding under the relevant Sub-Classes of Wrapped Bonds. If no such election is made, the Financial Guarantor will continue to be liable to make payments in respect of the Bonds pursuant to the relevant Financial Guarantee on the dates on which such payments would have been required to be made if such amounts had not become immediately due and payable.

To the extent that the early redemption price of any Bonds exceeds the aggregate of the Principal Amount Outstanding of and any accrued interest outstanding on any such Bonds to be redeemed (each as adjusted for indexation in accordance with Condition 7(b) (*Application of the Index Ratio*), if applicable), payment of such early redemption price will not be guaranteed by the Financial Guarantor under the relevant Financial Guarantee.

(d) Status of Financial Guarantee

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

The relevant Financial Guarantee provided by the Financial Guarantor in respect of the Bonds will constitute a direct, unsecured obligation of the Financial Guarantor which will rank at least *pari passu* with all other unsecured obligations of such Financial Guarantor, save for such obligations as may be preferred by provisions of law that are both mandatory and of general application.

(e) Security Trustee not responsible for monitoring compliance

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

The Security Trustee shall not be responsible for monitoring compliance by SWS with any of its obligations under the Finance Documents to which it is a party except by means of receipt from SWS of certificates of compliance which SWS has covenanted to deliver to the Security Trustee pursuant to the provisions of the Common Terms Agreement and which will state among other things, that no Default is outstanding. The Security Trustee shall be entitled to rely on certificates absolutely unless it is instructed otherwise by the Majority Creditors in which case it will be bound to act on such instructions in accordance with the STID. The Security Trustee is not responsible for monitoring compliance by any of the parties with their respective obligations under the Finance Documents. The Security Trustee may call for and is at liberty to accept as sufficient evidence a certificate signed by any two Authorised Signatories of any Obligor or any other party to any Finance Document to the effect that any particular dealing, transaction, step or thing is in the opinion of the persons so certifying suitable or expedient or as to any other fact or matter upon which the Security Trustee may require to be satisfied. The Security Trustee is in no way bound to call for further evidence or be responsible for any loss that may be occasioned by acting on any such certificate although the same may contain some error or is not authentic. The

Security Trustee is entitled to rely upon any certificate believed by it to be genuine and will not be liable for so acting.

All Bondholders shall (on providing sufficient evidence of identity) be entitled to view a copy of the Periodic Information (as defined in the Master Definitions Agreement) as and when available to the Security Trustee pursuant to the terms of the CTA and to view a copy of the unaudited interim accounts and audited annual accounts of SWS within 60 days of 30 September and 120 days of 31 March, respectively.

In addition, each Guarantor has covenanted to provide the Security Trustee with certain additional information (as set out in Schedule 5, Part 1 "Information Covenants" of the Common Terms Agreement). Such information may be published on a website designated by the relevant Guarantor and the Security Trustee. Any Bondholder who provides sufficient evidence of identity may obtain the current password to such website upon application to the Principal Paying Agent or the Registrar (as applicable).

In the event the relevant website cannot be accessed or is infected by an electronic virus or function software for a period of five consecutive days, all such information set out above which would otherwise be available will be delivered to the Security Trustee in paper form for onward delivery to the Bond Trustee and the Agents. Copies of such information will be available for inspection at the specified office of the Agents and the Bond Trustee.

4 Security, Priority and Relationship with Secured Creditors

(a) Guarantee and Security

Under the Security Agreement, each of SWS Holdings Limited ("**SWSH**") and SWS Group Holdings Limited ("**SWSGH**") guarantees the obligations of each other Obligor under the Finance Documents and SWS and the Issuer will guarantee the obligations of each other under the Finance Documents, in each case to the Security Trustee for itself and on behalf of the Secured Creditors (including, without limitation, the Bond Trustee for itself and on behalf of the Bondholders) and secures such obligations upon the whole of its property, undertaking, rights and assets, subject to certain specified exceptions and, in the case of SWS, to the terms of the Instrument of Appointment (as defined below) and any requirements thereunder or the Act (as defined below). There is no intention to create further security for the benefit of the holders of Bonds issued after the Initial Issue Date. All Bonds issued by the Issuer under the Programme and any additional creditor of the Issuer acceding to the STID will share in the security (the "**Security**") constituted by the Security Documents.

In these Conditions:

the "**Act**" means the United Kingdom Water Industry Act 1991 (as amended);

"Instrument of Appointment" means the instrument of appointment, dated 1989 as amended under which the Secretary of State for the Environment appointed SWS as a water and sewerage undertaker under the Act for the areas described in the Instrument of Appointment, as modified or amended from time to time; and

"Obligors" means SWS, SWSGH, SWSH and the Issuer.

(b) *Relationship among Bondholders and with other Secured Creditors.*

The Bond Trust Deed contains provisions detailing the Bond Trustee's obligations to consider discretions of the Bond Trustee (except where expressly provided or otherwise referred to in Condition 16 (*Bond Trustee Projections*).

The STID provides that the Security Trustee (except in relation to its Reserved Matters and Entrenched Rights (each as defined in the Master Definitions Agreement) and subject to certain exceptions) will act on instructions of the Majority Creditors (including the Bond Trustee as trustee for and representative of the holders of each Sub-Class of Wrapped Bonds (following the occurrence of an FG Event of Default (as defined in the Master Definitions Agreement) in respect of the Financial Guarantor of such Wrapped Bonds which is continuing) and the holders of Unwrapped Bonds) and, when so doing, the Security Trustee is not required to have regard to the interests of any Secured Creditor (including the Bond Trustee as trustee for and representative of the Bondholders or any individual Bondholder) in relation to the exercise of such rights and, consequently, has no liability to the Bondholders as a consequence of so acting.

(c) *Enforceable Security*

In the event of the Security becoming enforceable as provided in the STID, the Security Trustee shall, if instructed by the Majority Creditors, enforce its rights with respect to the Security, but without any liability as to the consequence of such action and without having regard to the effect thereof on, or being required to account for such action to, any particular Bondholder, provided that the Security Trustee shall not be obliged to take any action unless it is indemnified and/or secured to its satisfaction.

(d) *Application After Enforcement*

After enforcement of the Security, the Security Trustee shall (to the extent that such funds are available) use funds standing to the credit of the Accounts (other than the Excluded Accounts) (each as defined in the Master Definitions Agreement) to make payments in accordance with the Payment Priorities (as set out in the Common Terms Agreement).

(e) *Bond Trustee and Security Trustee not liable for security*

The Bond Trustee and the Security Trustee will not be liable for any failure to make the usual investigations or any investigations which might be made by a

security holder in relation to the property which is the subject of the Security, and shall not be bound to enquire into or be liable for any defect or failure in the right or title of the relevant Obligor to the Security, whether such defect or failure was known to the Bond Trustee or the Security Trustee or might have been discovered upon examination or enquiry or whether capable of remedy or not, nor will it have any liability for the enforceability of the Security created under the Security Documents whether as a result of any failure, omission or defect in registering or filing or otherwise protecting or perfecting such Security. The Bond Trustee and the Security Trustee have no responsibility for the value of any such Security.

5 Issuer Covenants

So long as any of the Bonds remain outstanding, the Issuer has agreed to comply with the covenants as set out in Schedule 5 of the Common Terms Agreement.

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

6 Interest and other Calculations

(a) Interest Rate and Accrual

Each Bond (unless specified in the relevant Final Terms to be a Zero Coupon Bond) bears interest on its Principal Amount Outstanding as defined below (or as otherwise specified in the relevant Final Terms) from the Interest Commencement Date (as defined below) at the Interest Rate (as defined below), such interest being payable in arrear (unless otherwise specified in the relevant Final Terms) on each Interest Payment Date (as defined below).

Interest will cease to accrue on each Bond (or, in the case of the redemption of part only of a Bond, that part only of such Bond) on the due date for redemption unless, upon due presentation, payment of principal is improperly withheld or refused, in which event interest will continue to accrue (both before and after judgment) at the Interest Rate in the manner provided in this Condition 6 to the Relevant Date (as defined in Condition 6(i)*(Definitions)).*

In the case of interest on Class B Unwrapped Bonds only, if, on any Interest Payment Date, prior to the taking of Enforcement Action after the termination of a Standstill Period, there are insufficient funds available to the Issuer (after taking into account any amounts available to be drawn under any DSR Liquidity Facility or from the Debt Service Reserve Account) to pay such accrued interest, the Issuer's liability to pay such accrued interest will be treated as not having fallen due and will be deferred until the earliest of: (i) the next following Interest Payment Date on which the Issuer has, in accordance with the cash management provisions of Schedule 12 of the Common Terms Agreement, sufficient funds available to pay such deferred amounts (including any interest accrued thereon);

(ii) the date on which the Class A Debt has been paid in full; and (iii) an Acceleration of Liabilities (other than a Permitted Hedge Termination or a Permitted Lease Termination) and in the case of a Permitted Share Pledge Acceleration only to the extent that there would be sufficient funds available in accordance with the Payment Priorities to pay such deferred interest (including any interest accrued thereon). Interest will accrue on such deferred interest at the rate otherwise payable on unpaid principal of such Class B Unwrapped Bonds.

If any Maximum Interest Rate or Minimum Interest Rate is specified in the relevant Final Terms, then the Interest Rate shall in no event be greater than the maximum or be less than the minimum so specified, as the case may be.

(b) *Business Day Convention*

If any date referred to in these Conditions or the relevant Final Terms is specified to be subject to adjustment in accordance with a Business Day convention and would otherwise fall on a day which is not a Business Day (as defined below), then if the Business Day Convention specified in the relevant Final Terms is:

(i) the "**Following Business Day Convention**", such date shall be postponed to the next day which is a Business Day;

(ii) the **"Modified Following Business Day Convention",** such date shall be postponed to the next day which is a Business Day unless it would thereby fall into the next calendar month, in which event such date shall be brought forward to the immediately preceding Business Day; or

(iii) the **"Preceding Business Day Convention"**, such date shall be brought forward to the immediately preceding Business Day.

(c) *Floating Rate Bonds*

This Condition 6(c) is applicable only if the relevant Final Terms specify the Bonds as Floating Rate Bonds.

If **"Screen Rate Determination"** is specified in the relevant Final Terms as the manner in which the Interest Rate(s) is/are to be determined, the Interest Rate applicable to the Bonds for each Interest Period will be determined by the Agent Bank (or the Calculation Agent, if applicable) on the following basis:

(i) if the Page (as defined below) displays a rate which is a composite quotation or customarily supplied by one entity, the Agent Bank (or the Calculation Agent, if applicable) will determine the Relevant Rate (as defined in Condition 6(i) **(***Definitions***)**);

(ii) in any other case, the Agent Bank (or the Calculation Agent, if applicable) will determine the arithmetic mean of the Relevant Rates (as defined

below) which appear on the Page as of the Relevant Time (as defined below) on the relevant Interest Determination Date;

(iii) if, in the case of (i) above, such rate does not appear on that Page or, in the case of (ii) above, fewer than two such rates appear on that Page or if, in either case, the Page is unavailable, the Agent Bank (or the Calculation Agent, if applicable) will:

(a) request the principal Relevant Financial Centre office of each of the Reference Banks (as defined in Condition 6(i) *(Definitions))* to provide a quotation of the Relevant Rate at approximately the Relevant Time on the relevant Interest Determination Date to prime banks in the Relevant Financial Centre (as defined below) interbank market (or, if appropriate, money market) in an amount that is representative for a single transaction in that market at that time; and

(b) determine the arithmetic mean of such quotations; and

(iv) if fewer than two such quotations are provided as requested in Condition 6(c)(iii), the Agent Bank (or the Calculation Agent, if applicable) will determine the arithmetic mean of the rates (being the rates nearest to the Relevant Rate as determined by the Agent Bank (or the Calculation Agent, if applicable)) quoted by the Reference Banks at approximately 11.00 a.m. (local time in the Relevant Financial Centre of the Relevant Currency) on the first day of the relevant Interest Period (as defined in Condition 6(i) *(Definitions))* for loans in the Relevant Currency to leading European banks for a period equal to the relevant Interest Period and in the Representative Amount (as defined in Condition 6(i) *(Definitions)).*

and the Interest Rate for such Interest Period shall be the sum of the Margin and the rate or (as the case may be) the arithmetic mean so determined. However, if the Agent Bank is unable to determine a rate or (as the case may be) an arithmetic mean in accordance with the above provisions in relation to any Interest Period, the Interest Rate applicable to the Bonds during such Interest Period will be the sum of the Margin and the rate or (as the case may be) the arithmetic mean last determined in relation to the Bonds in respect of a preceding Interest Period.

If **"ISDA Determination"** is specified in the relevant Final Terms as the manner in which the Interest Rate(s) is/are to be determined, the Interest Rate(s) applicable to the Bonds for each Interest Period will be the sum of the Margin and the relevant ISDA Rate where "**ISDA Rate**" in relation to any Interest Period means a rate equal to the Floating Rate (as defined in the ISDA Definitions) that would be determined by the Agent Bank (or the Calculation Agent, if applicable) under an interest rate swap transaction if the Agent Bank (or the Calculation Agent, if applicable) were acting as calculation agent for that interest rate swap

transaction under the terms of an agreement incorporating the ISDA Definitions and under which:

(i) the Floating Rate Option (as defined in the ISDA Definitions) is as specified in the relevant Final Terms;

(ii) the Designated Maturity (as defined in the ISDA Definitions) is the Specified Duration (as defined in Condition 6(i) (*Definitions*)); and

(iii) the relevant Reset Date (as defined in the ISDA Definitions) is either (1) if the relevant Floating Rate Option is based on LIBOR for a currency, the first day of that Interest Period, (2) if the relevant Floating Rate Option is based on EURIBOR, the first day of that Interest Period or (3) in any other case, as specified in the relevant Final Terms.

(d) Fixed Rate Bonds

This Condition 6(d) is applicable only if the relevant Final Terms specify the Bonds as Fixed Rate Bonds.

The Interest Rate applicable to the Bonds for each Interest Period will be the rate specified in the relevant Final Terms.

(e) Indexed Bonds

This Condition 6(e) is applicable only if the relevant Final Terms specify the Bonds as Indexed Bonds.

Payments of principal on, and the interest payable in respect of, the Bonds will be subject to adjustment for indexation and to the extent set out in Condition 7(b) *(Application of the Index Ratio).* The Interest Rate applicable to the Bonds for each Interest Period will be at the rate specified in the relevant Final Terms.

(f) Rounding

For the purposes of any calculations required pursuant to these Conditions (unless otherwise specified):

(i) all percentages resulting from such calculations will be rounded, if necessary, to he nearest one hundred-thousandth of a percentage point (with halves being rounded up);

(ii) all figures will be rounded to seven significant figures (with halves being rounded up); and

(iii) all currency amounts which fall due and payable will be rounded to the nearest unit of such currency (with halves being rounded up). For these purposes, "unit" means, with respect to any currency other than euro, the

lowest amount of such currency which is available as legal tender in the country of such currency and, with respect to euro, means 0.01 euro.

(g) *Calculations*

The amount of interest payable in respect of any Bond for each Interest Period shall be calculated by multiplying the product of the Interest Rate and the Principal Amount Outstanding of such Bond during that Interest Period by the Day Count Fraction (as defined in Condition 6(i) *(Definitions))* and, in the case of Indexed Bonds only, adjusted according to the indexation set out in Condition 7(b) (*Application of the Index Ratio*), unless an Interest Amount is specified in respect of such period in the relevant Final Terms, in which case the amount of interest payable in respect of such Bond for such Interest Period will equal such Interest Amount.

(h) *Determination and Publication of Interest Rates, Interest Amounts, Redemption Amounts and Instalment Amounts*

As soon as practicable after the Relevant Time on each Interest Determination Date or such other time on such date as the Agent Bank (or the Calculation Agent, if applicable) may be required to calculate any Redemption Amount or the amount of an instalment of scheduled principal (an "**Instalment Amount**"), obtain any quote or make any determination or calculation, the Agent Bank (or the Calculation Agent, if applicable) will determine the Interest Rate and calculate the amount of interest payable (the "**Interest Amounts**") in respect of each Specified Denomination of Bonds for the relevant Interest Period (including, for the avoidance of doubt any applicable Index Ratio to be calculated in accordance with Condition 7(b) (*Application of the Index Ratio*), calculate the Redemption Amount or Instalment Amount, obtain such quote or make such determination or calculation, as the case may be, and cause the Interest Rate and the Interest Amounts for each Interest Period and the relevant Interest Payment Date and, if required to be calculated, the Redemption Amount, Principal Amount Outstanding or any Instalment Amount to be notified to, in the case of Bearer Bonds, the Paying Agents or in the case of Registered Bonds, the Registrar, and, in each case, the Bond Trustee, the Issuer, the Bondholders and the London Stock Exchange and each other listing authority, stock exchange and/or quotation system by which the relevant Bonds have then been admitted to listing, trading and/or quotation) as soon as possible after its determination but in no event later than (i) (in case of notification to the London Stock Exchange and each other listing authority, stock exchange and/or quotation system by which the relevant Bonds have then been admitted to listing, trading and/or quotation) the commencement of the relevant Interest Period, if determined prior to such time, in the case of an Interest Rate and Interest Amount, or (ii) in all other cases, the fourth Business Day after such determination. The Interest Amounts and the Interest Payment Date so published may subsequently be amended (or appropriate alternative arrangements made by way of adjustment) without notice in the event of an extension or shortening of the Interest Period. Any such amendment will be

promptly notified to each stock exchange or other relevant authority on which the relevant Sub-Class or Class of Bonds are for the time being listed or by which they have been admitted to listing and to the Bondholders in accordance with Condition 17 (*Notices).* If the Bonds become due and payable under Condition 11 *(Events of Default*), the accrued interest and the Interest Rate payable in respect of the Bonds shall nevertheless continue to be calculated as previously provided in accordance with this Condition but no publication of the Interest Rate or the Interest Amount so calculated need be made unless otherwise required by the Bond Trustee. The determination of each Interest Rate, Interest Amount, Redemption Amount and Instalment Amount, the obtaining of each quote and the making of each determination or calculation by the Agent Bank (or the Calculation Agent, if applicable) or, as the case may be, the Bond Trustee pursuant to this Condition 6 or Condition 7 (*Indexation),* shall (in the absence of manifest error) be final and binding upon all parties.

(i) *Definitions*

In these Conditions, unless the context otherwise requires, the following defined terms shall have the meanings set out below.

"Business Day" means:

(i) in relation to any sum payable in euro, a TARGET Settlement Day and a day on which commercial banks and foreign exchange markets settle payments generally in London and each (if any) additional city or cities specified in the relevant Final Terms; and

(ii) in relation to any sum payable in a currency other than euro, a day on which commercial banks and foreign exchange markets settle payments generally in London, in the principal financial centre of the Relevant Currency (which in the case of a payment in U.S. Dollars shall be New York) and in each (if any) additional city or cities specified in the relevant Final Terms.

"Day Count Fraction" means, in respect of the calculation of an amount of interest on any Bond for any period of time (whether or not constituting an Interest Period, the "**Calculation Period**"):

(i) if "**Actual/Actual (ICMA)**" is specified:

(a) if the Calculation Period is equal to or shorter than the Determination Period during which it falls, the number of days in the Calculation Period divided by the product of (x) the number of days in such Determination Period and (y) the number of Determination Periods normally ending in any year; and

(b) if the Calculation Period is longer than one Determination Period, the sum of;

(x) the number of days in such Calculation Period falling in the Determination Period in which it begins divided by the product of (1) the number of days in such Determination Period and (2) the number of Determination Periods normally ending in any year; and

(y) the number of days in such Calculation Period falling in the next Determination Period divided by the product of (1) the number of days in such Determination Period and (2) the number of Determination Periods normally ending in any year,

where:

"Determination Period" means the period from and including a Determination Date in any year but excluding the next Determination Date; and

"Determination Date" means the date specified as such hereon or, if none is so specified, the Interest Payment Date;

(ii) if **"Actual/365"** or **"Actual/Actual"** is specified, the actual number of days in the Calculation Period divided by 365 (or, if any portion of that Calculation Period falls in a leap year, the sum of (1) the actual number of days in that portion of the Calculation Period falling in a leap year divided by 366, and (2) the actual number of days in that portion of the Calculation Period falling in a non-leap year divided by 365);

(iii) if **"Actual/365 (Fixed)"** is specified, the actual number of days in the Calculation Period divided by 365;

(iv) if **"Actual/360"** is specified, the actual number of days in the Calculation Period divided by 360;

(v) if **"30/360", "360/360"** or **"Bond Basis"** is specified, the number of days in the Calculation Period divided by 360 (the number of days to be calculated on the basis of a year of 360 days with 12 30-day months (unless (1) the last day of the Calculation Period is the 31st day of a month but the first day of the Calculation Period is a day other than the 30th or 31st of a month, in which case the month that includes that last day shall not be considered to be shortened to a 30-day month, or (2) the last day of the Calculation Period is the last day of the month of February, in which case the month of February shall not be considered to be lengthened to a 30-day month)); and

(vi) if **"30E/360"** or "**Eurobond Basis"** is specified, the number of days in the Calculation Period divided by 360 (the number of days to be calculated on the basis of a year of 360 days with 12 30-day months, without regard to

the date of the first day or last day of the Calculation Period unless, in the case of the final Calculation Period, the last day of such period is the last day of the month of February, in which case the month of February shall not be considered to be lengthened to a 30 day month);

"euro" means the lawful currency of the Participating Member States;

"Interest Commencement Date" means the Issue Date or such other date as may be specified in the relevant Final Terms;

"Interest Determination Date" means, with respect to an Interest Rate and an Interest Period, the date specified as such in the relevant Final Terms or, if none is so specified, the day falling two Business Days in London prior to the first day of such Interest Period (or if the specified currency is sterling the first day of such Interest Period) (as adjusted in accordance with any Business Day Convention (as defined below) specified in the relevant Final Terms);

"Interest Payment Date" means the date(s) specified as such in the relevant Final Terms;

"Interest Period" means the period beginning on (and including) the Interest Commencement Date and ending on (but excluding) the first Interest Payment Date and each successive period beginning on (and including) an Interest Payment Date and ending on (but excluding) the next succeeding Interest Payment Date;

"Interest Rate" means the rate of interest payable from time to time in respect of the Bonds and which is either specified as such in, or calculated in accordance with the provisions of, these Conditions and/or the relevant Final Terms;

"ISDA Definitions" means the 2000 ISDA Definitions (as amended and updated as at the date of issue of the first Tranche of Bonds of the relevant Sub-Class as published by the International Swaps and Derivatives Association, Inc.);

"Issue Date" means the date specified as such in the relevant Final Terms;

"Margin" means the rate per annum (expressed as a percentage) specified as such in the relevant Final Terms;

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

"Page" means such page, section, caption, column or other part of a particular information service (including the Reuters Money 3000 Service ("**Reuters**") and the Telerate Monitor Screen ("**Telerate**")) as may be specified in the relevant Final Terms, or such other page, section, caption, column or other part as may replace the same on that information service or on such other information service, in each case as may be nominated by the person or organisation providing or

sponsoring the information appearing there for the purpose of displaying comparable rates or prices;

"Participating Member State" means a Member State of the European Communities which adopts the euro as its lawful currency in accordance with the Treaty establishing the European Communities (as amended), and **"Participating Member States"** means all of them;

"Principal Amount Outstanding" means, in relation to a Bond, Sub-Class or Class, the original face value thereof less any repayment of principal made to the Holder(s) thereof in respect of such Bond, Sub-Class or Class;

"Redemption Amount" means the amount provided under Condition 8(b) (*Optional Redemption*), unless otherwise specified in the relevant Final Terms;

"Reference Banks" means the institutions specified as such or, if none, four major banks selected by the Agent Bank (or the Calculation Agent, if applicable) in the interbank market (or, if appropriate, money market) which is most closely connected with the Relevant Rate as determined by the Agent Bank (or the Calculation Agent, if applicable), on behalf of the Issuer, in its sole and absolute discretion;

"Relevant Currency" means the currency specified as such or, if none is specified, the currency in which the Bonds are denominated;

"Relevant Date" means the earlier of (a) the date on which all amounts in respect of the Bonds have been paid, and (b) five days after the date on which all of the Principal Amount Outstanding (adjusted in the case of Indexed Bonds in accordance with Condition 7(b) (*Application of Index Ratio*)) has been received by the Principal Paying Agent or the Registrar, as the case may be. and notice to that effect has been given to the Bondholders in accordance with Condition 17 *(Notices);*

"Relevant Financial Centre" means, with respect to any Bond, the financial centre specified as such in the relevant Final Terms or, if none is so specified, the financial centre with which the Relevant Rate is most closely connected as determined by the Agent Bank (or the Calculation Agent, if applicable);

"Relevant Rate" means the offered rate for a Representative Amount of the Relevant Currency for a period (if applicable) equal to the Specified Duration (or such other rate as shall be specified in the relevant Final Terms);

"Relevant Time" means, with respect to any Interest Determination Date, the local time in the Relevant Financial Centre specified in the relevant Final Terms or, if none is specified, the local time in the Relevant Financial Centre at which it is customary to determine bid and offered rates in respect of deposits in the Relevant Currency in the interbank market in the Relevant Financial Centre;

"Representative Amount" means, with respect to any rate to be determined on an Interest Determination Date, the amount specified in the relevant Final Terms as such or, if none is specified, an amount that is representative for a single transaction in the relevant market at the time;

"**Specified Duration**" means, with respect to any Floating Rate (as defined in the ISDA Definitions) to be determined on an Interest Determination Date, the period or duration specified as such in the relevant Final Terms or, if none is specified, a period of time equal to the relative Interest Period;

"TARGET Settlement Day" means any day on which the TARGET system is open; and

"TARGET system" means the Trans-European Automated Real-Time Gross Settlement Express Transfer system.

(j) *Agent Bank, Calculation Agent and Reference Banks*

The Issuer will procure that there shall at all times be an Agent Bank (and a Calculation Agent, if applicable) and four Reference Banks selected by the Issuer acting through the Agent Bank (or the Calculation Agent, if applicable) with offices in the Relevant Financial Centre if provision is made for them in these Conditions applicable to this Bond and for so long as it is outstanding. If any Reference Bank (acting through its relevant office) is unable or unwilling to continue to act as a Reference Bank, then the Issuer acting through the Agent Bank (or the Calculation Agent, if applicable) will select another Reference Bank with an office in the Relevant Financial Centre to act as such in its place. If the Agent Bank (or the Calculation Agent, if applicable) is unable or unwilling to act as such or if the Agent Bank (or the Calculation Agent, if applicable) fails duly to establish the Interest Rate for any Interest Period or to calculate the Interest Amounts or any other requirements, the Issuer will appoint (with the prior written consent of the Bond Trustee) a successor to act as such in its place. The Agent Bank may not resign its duties without a successor having been appointed as aforesaid.

(k) *Determination or Calculation by Bond Trustee*

If the Agent Bank (or the Calculation Agent, if applicable) does not at any time for any reason determine any Interest Rate, Interest Amount, Redemption Amount, Instalment Amount or any other amount to be determined or calculated by it, the Bond Trustee shall (without liability for so doing) determine such Interest Rate. Interest Amount, Redemption Amount, Instalment Amount or other amount as aforesaid at such rate or in such amount as in its absolute discretion (having regard as it shall think fit to the procedures described above, but subject to the terms of the Bond Trust Deed) it shall deem fair and reasonable in all the circumstances or, subject as aforesaid, apply the foregoing provisions of this Condition, with any consequential amendments, to the extent that, in its sole

opinion, it can do so and in all other respects it shall do so in such manner as it shall, in its absolute discretion, deem fair and reasonable in the circumstances, and each such determination or calculation shall be deemed to have been made by the Agent Bank (or the Calculation Agent, if applicable).

(l) *Certificates to be final*

All certificates, communications, opinions, determinations, calculations, quotations and decisions given, expressed, made or obtained for the purposes of the provisions of Condition 6 (*Interest and Other Calculations*) whether by the Principal Paying Agent, the Agent Bank (or the Calculation Agent, if applicable) or, if applicable, any calculation agent, shall (in the absence of wilful default, negligence, bad faith or manifest error) be binding on the Issuer, SWS, SWSH, SWSGH, the Agent Bank, the Bond Trustee, the Principal Paying Agent, the other Agents and all Bondholders, Receiptholders and Couponholders and (in the absence as aforesaid) no liability to the Issuer, SWS, SWSH, SWSGH, the Bond Trustee, the Bondholders, the Receiptholders or the Couponholders shall attach to the Principal Paying Agent, the Agent Bank or, if applicable, any calculation agent in connection with the exercise or non-exercise by it of its powers, duties and discretions pursuant to such provisions.

(m) *Interest on Dual Currency Bonds*

The rate or amount of interest payable in respect of Dual Currency Bonds shall be determined in the manner specified in the applicable Final Terms.

(n) *Interest on Partly Paid Bonds*

In the case of Partly Paid Bonds (other than Partly Paid Bonds which are Zero Coupon Bonds), interest will accrue as aforesaid on the paid-up nominal amount of such Bonds and otherwise as specified in the applicable Final Terms.

7 Indexation

This Condition 7 is applicable only if the relevant Final Terms specify the Bonds as Indexed Bonds.

(a) *Definitions*

"affiliate" means in relation to any person, any entity controlled, directly or indirectly, by that person, any entity that controls directly or indirectly, that person or any entity, directly or indirectly under common control with that person and, for this purpose, "**control**" means control as defined in the Companies Act 1985;

"Base Index Figure" means (subject to Condition 7(c)(i) (*Change in base*)) the base index figure as specified in the relevant Final Terms;

“Index” or **“Index Figure”** means, subject as provided in Condition 7(c)(i) (*Change in base*), the UK Retail Price Index (RPI) (for all items) published by the Central Statistical Office (January 1987 = 100) or any comparable index which may replace the UK Retail Price Index for the purpose of calculating the amount payable on repayment of the Reference Gilt. Any reference to the Index Figure applicable to a particular month shall, subject as provided in Condition 7(c) (*Changes in Circumstances Affecting the Index*) and (e) (*Cessation of or Fundamental Changes to the Index*), be construed as a reference to the Index Figure published in the seventh month prior to that particular month and relating to the month before that of publication. If the Index is replaced, the Issuer will describe the replacement Index in a supplementary prospectus;

“Index Ratio” applicable to any month means the Index Figure applicable to such month divided by the Base Index Figure;

“Limited Index Ratio” means (a) in respect of any month prior to the relevant Issue Date, the Index Ratio for that month; (b) in respect of any Limited Indexation Month after the relevant Issue Date, the product of the Limited Indexation Factor for that month and the Limited Index Ratio as previously calculated in respect of the month twelve months prior thereto; and (c) in respect of any other month, the Limited Index Ratio as previously calculated in respect of the most recent Limited Indexation Month;

“Limited Indexation Factor” means, in respect of a Limited Indexation Month, the ratio of the Index Figure applicable to that month divided by the Index Figure applicable to the month twelve months prior thereto, provided that (a) if such ratio is greater than the Maximum Indexation Factor specified in the relevant Final Terms, it shall be deemed to be equal to such Maximum Indexation Factor and (b) if such ratio is less than the Minimum Indexation Factor specified in the relevant Final Terms, it shall be deemed to be equal to such Minimum Indexation Factor;

“Limited Indexation Month” means any month specified in the relevant Final Terms for which a Limited Indexation Factor is to be calculated;

“Limited Indexed Bonds” means Indexed Bonds to which a Maximum Indexation Factor and/or a Minimum Indexation Factor (as specified in the relevant Final Terms) applies; and

“Reference Gilt” means the Treasury Stock specified as such in the relevant Final Terms for so long as such stock is in issue, and thereafter such issue of index-linked Treasury Stock determined to be appropriate by a gilt-edged market maker or other adviser selected by the Issuer and approved by the Bond Trustee (an “**Indexation Adviser**”).

(b) *Application of the Index Ratio*

Each payment of interest and principal in respect of the Bonds shall be the amount provided in, or determined in accordance with, these Conditions, multiplied by the

Index Ratio or Limited Index Ratio in the case of Limited Indexed Bonds applicable to the month in which such payment falls to be made and rounded in accordance with Condition 6(f) (*Rounding*).

(c) *Changes in Circumstances Affecting the Index*

(i) Change in base: If at any time and from time to time the Index is changed by the substitution of a new base therefor, then with effect from the calendar month from and including that in which such substitution takes effect (1) the definition of **"Index"** and **"Index Figure"** in Condition 7(a) (*Definitions*) shall be deemed to refer to the new date or month in substitution for January 1987 (or, as the case may be, to such other date or month as may have been substituted therefor), and (2) the new Base Index Figure shall be the product of the existing Base Index Figure (being at the Initial Issue Date 178.2) and the Index Figure immediately following such substitution, divided by the Index Figure immediately prior to such substitution.

(ii) Delay in publication of Index: If the Index Figure which is normally published in the seventh month and which relates to the eighth month (the "**relevant month**") before the month in which a payment is due to be made is not published on or before the fourteenth business day before the date on which such payment is due (the "**date for payment**"), the Index Figure applicable to the month in which the date for payment falls shall be (1) such substitute index figure (if any) as the Bond Trustee considers to have been published by the Bank of England for the purposes of indexation of payments on the Reference Gilt or, failing such publication, on any one or more issues of index-linked Treasury Stock selected by an Indexation Adviser (and approved by the Bond Trustee) or (2) if no such determination is made by such Indexation Adviser within seven days, the Index Figure last published (or, if later, the substitute index figure last determined pursuant to Condition 7(c)(i) (*Change in base*)) before the date for payment.

(d) *Application of Changes*

Where the provisions of Condition 7(c)(ii) (*Delay in publication of Index*) apply, the determination of the Indexation Adviser as to the Index Figure applicable to the month in which the date for payment falls shall be conclusive and binding. If, an Index Figure having been applied pursuant to Condition 7(c)(ii)(2), the Index Figure relating to the relevant month is subsequently published while a Bond is still outstanding, then:

(i) in relation to a payment of principal or interest in respect of such Bond other than upon final redemption of such Bond, the principal or interest (as the case may be) next payable after the date of such subsequent publication shall be increased or reduced by an amount equal to

(respectively) the shortfall or excess of the amount of the relevant payment made on the basis of the Index Figure applicable by virtue of Condition 7(c)(ii)(2), below or above the amount of the relevant payment that would have been due if the Index Figure subsequently published had been published on or before the fourteenth business day before the date for payment; and

(ii) in relation to a payment of principal or interest upon final redemption, no subsequent justment to amounts paid will be made.

(e) Cessation of or Fundamental Changes to the Index

(i) If (1) the Bond Trustee has been notified by the Agent Bank (or the Calculation Agent, if applicable) that the Index has ceased to be published or (2) any change is made to the coverage or the basic calculation of the Index which constitutes a fundamental change which would, in the opinion of the Bond Trustee acting solely on the advice of an Indexation Adviser, be materially prejudicial to the interests of the Bondholders, the Bond Trustee will give written notice of such occurrence to the Issuer, and the Issuer and the Bond Trustee together shall seek to agree for the purpose of the Bonds one or more adjustments to the Index or a substitute index (with or without adjustments) with the intention that the same should leave the Issuer and the Bondholders in no better and no worse position than they would have been had the Index not ceased to be published or the relevant fundamental change not been made.

(ii) If the Issuer and the Bond Trustee fail to reach agreement as mentioned above within 20 business days following the giving of notice as mentioned in paragraph (i), a bank or other person in London shall be appointed by the Issuer and the Bond Trustee or, failing agreement on and the making of such appointment within 20 business days following the expiry of the 20 day period referred to above, by the Bond Trustee (in each case, such bank or other person so appointed being referred to as the "**Expert**"), to determine for the purpose of the Bonds one or more adjustments to the Index or a substitute index (with or without adjustments) with the intention that the same should leave the Issuer and the Bondholders in no better and no worse position than they would have been had the Index not ceased to be published or the relevant fundamental change not been made. Any Expert so appointed shall act as an expert and not as an arbitrator and all fees, costs and expenses of the Expert and of any Indexation Adviser and of any of the Issuer and the Bond Trustee in connection with such appointment shall be borne by the Issuer.

(iii) The Index shall be adjusted or replaced by a substitute index as agreed by the Issuer and the Bond Trustee or as determined by the Expert pursuant to the foregoing paragraphs, as the case may be, and references in these Conditions to the Index and to any Index Figure shall be deemed amended

in such manner as the Bond Trustee and the Issuer agree are appropriate to give effect to such adjustment or replacement. Such amendments shall be effective from the date of such notification and binding upon the Issuer, the Financial Guarantor(s), the other Secured Creditors, the Bond Trustee and the Bondholders, and the Issuer shall give notice to the Bondholders in accordance with Condition 17 *(Notices)* of such amendments as promptly as practicable following such notification.

8 Redemption, Purchase and Cancellation

(a) Partial and Final Redemption

Unless previously redeemed, or purchased and cancelled as provided below, or unless such Bond is stated in the relevant Final Terms as having no fixed maturity date, each Bond will be redeemed at its Principal Amount Outstanding (in the case of Indexed Bonds as adjusted in accordance with Condition 7(b) *(Application of the Index Ratio)),* on the date or dates (or, in the case of Floating Rate Bonds, on the Interest Payment Date(s)) specified in the relevant Final Terms plus accrued but unpaid interest (other than in the case of Zero Coupon Bonds) and, in the case of Indexed Bonds as adjusted in accordance with Condition 7(b) *(Application of the Index Ratio).*

In the case of principal on Class B Unwrapped Bonds only, if on any date, prior to the taking of Enforcement Action after the termination of a Standstill Period, on which such Bond is to be redeemed (in whole of in part) there are insufficient funds available to the Issuer to pay such principal, the Issuer's liability to pay such principal will be treated as not having fallen due and will be deferred until the earliest of (i) the next following Interest Payment Date on which the Issuer has, in accordance with the cash management provisions of Schedule 12 of the Common Terms Agreement, sufficient funds to pay such deferred amounts (including any interest accrued thereon); (ii) the date on which all Class A Debt has been paid in full and (iii) an Acceleration of Liabilities (other than a Permitted Hedge Termination or a Permitted Lease Termination) and in the case of a Permitted Share Pledge Acceleration only to the extent that there would be sufficient funds available in accordance with the Payment Priorities to pay such deferred principal (including any accrued interest thereon). Interest will accrue on such deferred principal at the rate otherwise payable on unpaid principal of such Class B Unwrapped Bonds.

(b) Optional Redemption

Subject as provided below, upon giving not more than 60 nor less than 30 days' notice to the Bond Trustee, the Security Trustee, the Majority Creditors and the Bondholders, the Issuer may (prior to the Maturity Date) redeem any Sub-Class of the Bonds in whole or in part (but on a pro rata basis only) on any Interest Payment Date at their Redemption Amount, provided that Floating Rate Bonds

may not be redeemed before the date specified in the relevant Final Terms, as follows:

(i) In respect of Fixed Rate Bonds, the Redemption Amount will, unless otherwise specified in the relevant Final Terms, be an amount equal to the higher of (i) their Principal Amount Outstanding and (ii) the price determined to be appropriate by a financial adviser in London (selected by the Issuer and approved by the Bond Trustee) as being the price at which the Gross Redemption Yield (as defined below) on such Bonds on the Reference Date (as defined below) is equal to the Gross Redemption Yield at 3:00 p.m. (London time) on the Reference Date on the Reference Gilt (as defined below) while that stock is in issue, and thereafter such UK government stock as the Issuer may, with the advice of three persons operating in the gilt-edged market (selected by the Issuer and approved by the Bond Trustee) determine to be appropriate, plus accrued but unpaid interest on the Principal Amount Outstanding.

For the purposes of this Condition 8(b)(i), "**Gross Redemption Yield**" means a yield expressed as a percentage and calculated on a basis consistent with the basis indicated by the United Kingdom Debt Management Office publication "Formulae for Calculating Gilt Prices from Yields" published on 8 June 1998 with effect from 1 November 1998 and updated on 15 January 2002 page 5 or any replacement therefor; **"Reference Date"** means the date which is two Business Days prior to the despatch of the notice of redemption under this Condition 8(b)(i); and "**Reference Gilt**" means the Treasury Stock specified in the relevant Final Terms.

(ii) In respect of Floating Rate Bonds, the Redemption Amount will, unless otherwise specified in the relevant Final Terms, be the Principal Amount Outstanding plus any premium for early redemption in certain years (as specified in the relevant Final Terms) plus any accrued but unpaid interest on the Principal Amount Outstanding.

(iii) In respect of Indexed Bonds, the Redemption Amount will (unless otherwise specified in the relevant Final Terms) be the higher of (i) the Principal Amount Outstanding and (ii) the price determined to be appropriate (without any additional indexation beyond the implicit indexation in such determined price) by a financial adviser in London (selected by the Issuer and approved by the Bond Trustee as being the price at which the Gross Real Redemption Yield (as defined below) on the Bonds on the Reference Date (as defined below) is equal to the Gross Real Redemption Yield at 3:00 p.m. (London time) on the Reference Date on the Reference Gilt while that stock is in issue, and thereafter such UK government stock as the Issuer may, with the advice of three persons operating in the gilt-edged market, (selected by the Issuer and approved by the Bond Trustee), determine to be appropriate, plus accrued but unpaid

interest (as adjusted in accordance with Condition 7(b) (*Application of the Index Ratio*)) on the Principal Amount Outstanding.

For the purposes of this Condition 8(b)(iii), **"Gross Real Redemption Yield"** means a yield expressed as a percentage and calculated on a basis consistent with the basis indicated by the United Kingdom Debt Management Office publication "Formulae for Calculating Gilt Prices from Yields" published on 8 June 1998 with effect from 1 November 1998 and updated on 15 January 2002, page 4 or any replacement therefor, **"Reference Date"** means the date which is two Business Days prior to the despatch of the notice of redemption under this Condition 8(b)(iii); and **"Reference Gilt"** means the Treasury Stock specified in the relevant Final Terms.

In any such case, prior to giving any such notice, the Issuer must certify (as further specified in the Finance Documents) to the Bond Trustee that it will have the funds, not subject to any interest (other than under the Security) of any other person, required to redeem the Bonds as aforesaid.

(c) *Redemption for Index Event, Taxation or Other Reasons*

Redemption for Index Events: Upon the occurrence of any Index Event (as defined below), the Issuer may, upon giving not more than 60 nor less than 30 days' notice to the Bond Trustee, the Security Trustee, the Majority Creditors and the holders of the Indexed Bonds in accordance with Condition 17 *(Notices),* redeem all (but not some only) of the Indexed Bonds of all Sub-Classes on any Interest Payment Date at the Principal Amount Outstanding (adjusted in accordance with Condition 7(b) *(Application of Index Ratio)*) plus accrued but unpaid interest. No single Sub-Class of Indexed Bonds may be redeemed in these circumstances unless all the other Classes and Sub-Classes of Indexed Bonds are also redeemed at the same time. Before giving any such notice, the Issuer shall provide to the Bond Trustee, the Security Trustee, the Majority Creditors and the relevant Financial Guarantor(s) a certificate signed by an authorised signatory (a) stating that the Issuer is entitled to effect such redemption and setting forth a statement of facts showing that the conditions precedent to the right of the Issuer so to redeem have occurred and (b) confirming that the Issuer will have sufficient funds on such Interest Payment Date to effect such redemption.

"Index Event" means (i) if the Index Figure for three consecutive months falls to be determined on the basis of an Index Figure previously published as provided in Condition 7(c)(ii) *(Delay in publication of Index*) and the Bond Trustee has been notified by the Principal Paying Agent that publication of the Index has ceased or (ii) notice is published by Her Majesty's Treasury, or on its behalf, following a change in relation to the Index, offering a right of redemption to the holders of the Reference Gilt, and (in either case) no amendment or substitution of the Index has been advised by the Indexation Adviser to the Issuer and such circumstances are continuing.

Redemption for Taxation Reasons: In addition, if at any time the Issuer satisfies the Bond Trustee that the Issuer would, on the next Interest Payment Date, become obliged to deduct or withhold from any payment of interest or principal in respect of the Bonds (other than in respect of default interest), any amount for or on account of any present or future taxes, duties, assessments or governmental charges of whatever nature imposed, levied, collected, withheld or assessed by the United Kingdom or the Cayman Islands or any political subdivision thereof, or any other authority thereof or any change in the application or official interpretation of such laws or regulations, then the Issuer may, in order to avoid the relevant deductions or withholding, use its reasonable endeavours to arrange the substitutions of a company incorporated under another jurisdiction approved by the Bond Trustee as principal debtor under the Bonds and as lender under the Issuer/SWS Loan Agreements and as obligor under the Finance Documents upon satisfying the conditions for substitution of the Issuer as set out in the STID (and referred to in Condition 15 (*Meetings of Bondholders, Modification, Waiver and Substitution*)). If the Issuer is unable to arrange a substitution as described above having used reasonable endeavours to do so and, as a result, the relevant deduction or withholding is continuing then the Issuer may, upon giving not more than 60 nor less than 30 days' notice to the Bond Trustee, the Security Trustee, the Majority Creditors and the Bondholders in accordance with Condition 17 *(Notices),* redeem all (but not some only) of the Bonds on any Interest Payment Date at their Principal Amount Outstanding plus accrued but unpaid interest thereon (each adjusted, in the case of Indexed Bonds, in accordance with Condition 7(b) *(Application of the Index Ratio)).* Before giving any such notice of redemption, the Issuer shall provide to the Bond Trustee, the Security Trustee and the Majority Creditors and the relevant Financial Guarantors a certificate signed by an authorised signatory (a) stating that the Issuer is entitled to effect such redemption and setting forth a statement of facts showing that the conditions precedent to the right of the Issuer so to redeem have occurred and (b) confirming that the Issuer will have sufficient funds on such Interest Payment Date to discharge all its liabilities in respect of the Bonds and any amounts under the Security Agreement to be paid in priority to, or *pari passu* with, the Bonds under the Payment Priorities.

(d) Redemption on Prepayment of Issuer/SWS Loan Agreements

If SWS gives notice to the Issuer under an Issuer/SWS Loan Agreement that it intends to prepay all or part of any advance made under such Issuer/SWS Loan Agreement and such advance was funded by the Issuer from the proceeds of the issue of a Sub-Class of Bonds, the Issuer shall, upon giving not more than 60 nor less than 30 days' notice to the Bond Trustee, the Security Trustee, the Majority Creditors, the relevant Financial Guarantors and the Bondholders in accordance with Condition 17 *(Notices)* (where such advance is being prepaid in whole), redeem all of the Bonds of that Sub-Class or (where part only of such advance is being prepaid) the proportion of the relevant Sub-Class of Bonds which the proposed prepayment amount bears to the amount of the relevant advance. In the case of a voluntary prepayment, the relevant Bonds will be redeemed at their

Redemption Amount determined in accordance with Condition 8(b) *(Optional Redemption)* except that, in the case of Fixed Rate Bonds and Indexed Bonds, for the purposes of this Condition 8(d), **"Reference Date"** means the date two Business Days prior to the despatch of the notice of redemption given under this Condition 8(d), plus accrued but unpaid interest and, in the case of any other prepayment, the relevant Bonds will be redeemed at their Principal Amount Outstanding plus accrued but unpaid interest.

(e) *Early redemption of Zero Coupon Bonds*

Unless otherwise specified in the relevant Final Terms, the Redemption Amount payable on redemption of a Zero Coupon Bond at any time before the Maturity Date shall be an amount equal to the sum of:

(i) the Reference Price; and

(ii) the product of the Accrual Yield (compounded annually) being applied to the Reference Price from (and including) the Issue Date to (but excluding) the date fixed for redemption or (as the case may be) the date upon which the Bond becomes due and payable.

Where such calculation is to be made for a period which is not a whole number of years, the calculation in respect of the period of less than a full year shall be made on the basis of such Day Count Fraction as may be specified in the Final Terms for the purposes of this Condition 8(e) or, if none is so specified, a Day Count Fraction of 30/360.

In these Conditions, **"Accrual Yield"** and **"Reference Price"** and **"Zero Coupon Bond"** have the meanings given to them in the relevant Final Terms.

(f) *Purchase of Bonds*

The Issuer may, provided that no Event of Default has. occurred and is continuing, purchase Bonds (provided that all unmatured Receipts and Coupons and unexchanged Talons (if any) appertaining thereto are attached or surrendered therewith) in the open market or otherwise at any price. Any purchase by tender shall be made available to all Bondholders alike.

If not all the Bonds which are in registered form are to be purchased, upon surrender of the existing Individual Bond Certificate, the Registrar shall forthwith upon the written request of the Bondholder concerned issue a new Individual Bond Certificate in respect of the Bonds which are not to be purchased and despatch such Individual Bond Certificate to the Bondholder (at the risk of the Bondholder and to such address as the Bondholder may specify in such request).

While the Bonds are represented by a Global Bond or Global Bond Certificate (as defined below), the relevant Global Bond or Global Bond

Certificate will be endorsed to reflect the Principal Amount Outstanding of Bonds to be so redeemed or purchased.

(g) *Redemption by Instalments*

Unless previously redeemed, purchased and cancelled as provided in this Condition 8, each Bond which provides for Instalment Dates (as specified in the relevant Final Terms) and Instalment Amounts (as specified in the relevant Final Terms) will be partially redeemed on each Instalment Date at the Instalment Amount.

(h) *Cancellation*

In respect of all Bonds purchased by or on behalf of the Issuer, the Bearer Bonds or the Registered Bonds shall be surrendered to or to the order of the Principal Paying Agent or the Registrar, as the case may be, for cancellation and, if so surrendered, will, together with all Bonds redeemed by the Issuer, be cancelled forthwith (together with, in the case of Bearer Bonds, all unmatured Receipts and Coupons and unexchanged Talons attached thereto or surrendered therewith). Any Bonds so surrendered for cancellation may not be reissued or resold and the obligations of the Issuer in respect of any such Bonds shall be discharged.

(i) *Instalments*

Instalment Bonds will be redeemed in the Instalment Amounts and on the Instalment Dates. In the case of early redemption, the Redemption Amount will be determined pursuant to paragraph (b) above.

(j) *Partly Paid Bonds*

Partly Paid Bonds will be redeemed, whether at maturity, early redemption or otherwise, in accordance with the provisions of this Condition and the applicable Final Terms.

9 Payments

(a) *Bearer Bonds*

Payments to the Bondholders of principal (or, as the case may be. Redemption Amounts or other amounts payable on redemption) and interest (or, as the case may be, Interest Amounts) in respect of Bearer Bonds will, subject as mentioned below, be made against presentation and surrender of the relevant Receipts (in the case of payment of Instalment Amounts other than on the due date for final redemption and provided that the Receipt is presented for payment together with its relative Bond), Bonds (in the case of all other payments of principal and, in the case of interest, as specified in Condition 9(f) *(Unmatured Coupons and Receipts and Unexchanged Talons))* or Coupons (in the case of interest, save as specified in Condition 9(f) *(Unmatured Coupons and Receipts and Unexchanged Talons)),*

as the case may be, at the specified office of any Paying Agent outside the United States of America by transfer to an account denominated in the currency in which such payment is due with, or (in the case of Bonds in definitive form only) a cheque payable in that currency drawn on, a bank in (i) the principal financial centre of that currency provided that such currency is not euro, or (ii) the principal financial centre of any Participating Member State if that currency is euro.

(b) *Registered Bonds*

Payments of principal (or, as the case may be, Redemption Amounts) in respect of Registered Bonds will be made to the holder (or the first named of joint holders) of such Bond against presentation and surrender of the relevant Registered Bond at the specified office of the Registrar and in the manner provided in Condition 9(a) *(Bearer Bonds).*

Payments of instalments in respect of Registered Bonds will be made to the holder (or the first named of joint holders) of such Bond against presentation of the relevant Registered Bond at the specified office of the Registrar in the manner provided in Condition 9(a) *(Bearer Bonds)* above and annotation of such payment on the Register and the relevant Bond Certificate.

Interest (or, as the case may be, Interest Amounts) on Registered Bonds payable on any Interest Payment Date will be paid to the holder (or the first named if joint holders) on the fifteenth day before the due date for payment thereof (the "**Record Date**"). Payment of interest or Interest Amounts on each Registered Bond will be made in the currency in which such payment is due by cheque drawn on a bank in (a) the principal financial centre of the country of the currency concerned, provided that such currency is not euro, or (b) the principal financial centre of any Participating Member State if that currency is euro and mailed to the holder (or to the first named of joint holders) of such Bond at its address appearing in the Register. Upon application by the Bondholder to the specified office of the Registrar before the relevant Record Date, such payment of interest may be made by transfer to an account in the relevant currency maintained by the payee with a bank in (a) the principal financial centre of the country of that currency provided that such currency is not euro, or (b) the principal financial centre of any Participating Member State if that currency is euro.

A record of each payment so made will be endorsed on the schedule to the Global Bond or the Global Bond Certificate by or on behalf of the Principal Paying Agent or the Registrar, as the case may be, which endorsement shall be prima facie evidence that such payment has been made.

(c) *Payments in the United States of America*

Notwithstanding the foregoing, if any Bearer Bonds are denominated in U.S. dollars, payments in respect thereof may be made at the specified office of any Paying Agent in New York City in the same manner as aforesaid if:

(i) the Issuer shall have appointed Paying Agents with specified offices outside the United States of America with the reasonable expectation that such Paying Agents would be able to make payment of the amounts on the Bonds in the manner provided above when due;

(ii) payment in full of such amounts at all such offices is illegal or effectively precluded by exchange controls or other similar restrictions on payment or receipt of such amounts; and

(iii) such payment is then permitted by the law of the United States of America, without involving, in the opinion of the Issuer, adverse tax consequences to the Issuer.

(d) Payments subject to fiscal laws; payments on Global Bonds and Registered Bonds

All payments are subject in all cases to any applicable fiscal or other laws, regulations and directives, but without prejudice to the provisions of this Condition 9. No commission or expenses shall be charged to the Bondholders, Couponholders or Receiptholders (if any) in respect of such payments.

The holder of a Global Bond or Global Bond Certificate shall be the only person entitled to receive payments of principal (or Redemption Amounts) and interest (or Interest Amounts) on the Global Bond or Global Bond Certificate (as the case may be) and the Issuer will be discharged by payment to, or to the order of, the holder of such Global Bond or Global Bond Certificate in respect of each amount paid.

(e) Appointment of the Agents

The Paying Agents, the Agent Bank, the Transfer Agents and the Registrar (the "**Agents**") appointed by the Issuer (and their respective specified offices) are listed in the Agency Agreement. Any Calculation Agent will be listed in the relevant Final Terms and will be appointed pursuant to a Calculation Agency Agreement. The Agents act solely as agents of the Issuer and do not assume any obligation or relationship of agency or trust for or with any holder. The Issuer reserves the right, with the prior written consent of the Bond Trustee at any time to vary or terminate the appointment of any Agent, and to appoint additional or other Agents, provided that the Issuer will at all times maintain (i) a Principal Paying Agent (in the case of Bearer Bonds), (ii) a Registrar (in the case of Registered Bonds), (iii) an Agent Bank or Calculation Agent (as specified in the relevant Final Terms) (in the case of Floating Rate Bonds or Indexed Bonds), (iv) a Paying Agent with a specified office in a European Union member state that will not be obliged to withhold or deduct tax pursuant to European Council Directive 2003/48/EC on the taxation of savings income or any law implementing or complying with, or introduced to conform to, such Directive; and (v) if and for so long as the Bonds are admitted to listing, trading and/or quotation by any listing authority, stock exchange and/or quotation system which requires the

appointment of a Paying Agent, Transfer Agent or Registrar in any particular place, a Paying Agent, Transfer Agent and/or Registrar, as applicable, having its specified office in the place required by such listing authority, stock exchange and/or quotation system, which, while any Bonds are admitted to the Official List of the UK Listing Authority and/or admitted to trading on the London Stock Exchange plc's Gilt-Edged and Fixed Interest Market or the London Stock Exchange plc's Professional Securities Market shall be in London. Notice of any such variation, termination or appointment will be given in accordance with Condition 17 *(Notices)*.

(f) *Unmatured Coupons and Receipts and Unexchanged Talons*

(i) Subject to the provisions of the relevant Final Terms, upon the due date for redemption of any Bond which is a Bearer Bond (other than a Fixed Rate Bond, unless it has all unmatured Coupons attached), unmatured Coupons and Receipts relating to such Bond (whether or not attached) shall become void and no payment shall be made in respect of them.

(ii) Upon the date for redemption of any Bond, any unmatured Talon relating to such Bond (whether or not attached) shall become void and no Coupon shall be delivered in respect of such Talon.

(iii) Upon the due date for redemption of any Bond which is redeemable in instalments, all Receipts relating to such Bond having an Instalment Date falling on or after such due date (whether or not attached) shall become void and no payment shall be made in respect of them.

(iv) Where any Bond, which is a Bearer Bond and is a Fixed Rate Bond, is presented for redemption without all unmatured Coupons and any unexchanged Talon relating to it, a sum equal to the aggregate amount of the missing unmatured Coupons will be deducted from the amount of principal due for payment and, redemption shall be made only against the provision of such indemnity as the Issuer may require.

(v) If the due date for redemption of any Bond is not an Interest Payment Date, interest accrued from the preceding Interest Payment Date or the Interest Commencement Date, as the case may be, or the Interest Amount payable on such date for redemption shall only be payable against presentation (and surrender if appropriate) of the relevant Bond and Coupon.

(g) *Non-Business Days*

Subject as provided in the relevant Final Terms, if any date for payment in respect of any Bond, Receipt or Coupon is not a business day, the holder shall not be entitled to payment until the next following business day nor to any interest or other sum in respect of such postponed payment. In this paragraph, "**business day**" means a day (other than a Saturday or a Sunday) on which banks are open

for presentation and payment of debt securities and for dealings in foreign currency in London and in the relevant place of presentation and in the cities referred to in the definition of Business Days and (in the case of a payment in a currency other than euro), where payment is to be made by transfer to an account maintained with a bank in the relevant currency, on which dealings may be carried on in the relevant currency in the principal financial centre of the country of such currency and, in relation to any sum payable in euro, a day on which the TARGET system is open.

(h) *Talons*

On or after the Interest Payment Date for the final Coupon forming part of a coupon sheet issued in respect of any Bond, the Talon forming part of such coupon sheet may be surrendered at the specified office of any Paying Agent in exchange for a further coupon sheet (and if necessary another Talon for a further coupon sheet) (but excluding any Coupons which may have become void pursuant to Condition 13 (*Prescription)).*

10 Taxation

All payments in respect of the Bonds, Receipts or Coupons will be made (whether by the Issuer, any Paying Agent, the Registrar, the Bond Trustee, the Security Trustee or, in respect of Wrapped Bonds, the Financial Guarantors) without withholding or deduction for, or on account of, any present or future taxes, duties or charges of whatsoever nature unless the Issuer, the Guarantors, any Paying Agent or the Registrar or, where applicable, the Bond Trustee, the Security Trustee or the Financial Guarantor is required by applicable law to make any payment in respect of the Bonds, Receipts or Coupons subject to any withholding or deduction for, or on account of, any present or future taxes, duties or charges of whatsoever nature. In that event, the Issuer, the Guarantors, such Paying Agent, the Registrar, the Bond Trustee, the Security Trustee or the Financial Guarantor, as the case may be, shall make such payment after such withholding or deduction has been made and shall account to the relevant authorities for the amount so required to be withheld or deducted. None of the Issuer, the Guarantors, any Paying Agent, the Registrar, the Bond Trustee, the Security Trustee or the Financial Guarantor will be obliged to make any additional payments to the Bondholders, Receiptholders or the Couponholders in respect of such withholding or deduction. The Issuer, the Guarantors, any Paying Agent, the Registrar, the Bond Trustee, the Security Trustee or the Financial Guarantor may require holders to provide such certifications and other documents as required by applicable law in order to qualify for exemptions from applicable tax laws.

If the Issuer is obliged to make any such deduction or withholding, the amount so deducted or withheld is not guaranteed by the Financial Guarantor.

11 Events of Default

The Events of Default (as defined in the Master Definitions Agreement) relating to the Bonds are set out in Schedule 7 of the Common Terms Agreement.

Following the notification of an Event of Default in respect of the Issuer, the STID provides for a Standstill Period (as defined in the Master Definitions Agreement) to commence and for restrictions to apply to all Secured Creditors of SWS. The Common Terms Agreement also contains various Trigger Events that will, if they occur, (among other things) permit the Majority Creditors to commission an Independent Review, require SWS to discuss its plans for appropriate remedial action and prevent the SWS Financing Group from making further Restricted Payments until the relevant Trigger Events have been remedied.

(a) Events of Default

If any Event of Default occurs and is continuing in relation to the Issuer, subject always to the terms of the STID, the Bond Trustee may at any time (in accordance with the provisions of the Bond Trust Deed and the STID), having certified in writing that in its opinion the happening of such event is materially prejudicial to the interests of the Bondholders and shall upon the Bond Trustee being so directed or requested (i) by an Extraordinary Resolution (as defined in the Bond Trust Deed) of holders of the relevant Sub-Classes of Class A Bonds or, if there are no Class A Bonds outstanding, the Class B Bonds or (ii) in writing by holders of at least one quarter in outstanding nominal amount of the relevant Sub-Classes of Class A Bonds, or if there are no Class A Bonds outstanding, the Class B Bonds and subject, in each case, to being indemnified and/or secured to its satisfaction, give notice to the Issuer and the Security Trustee that the Bonds of the relevant Sub-Class are, and they shall immediately become, due and repayable, at their respective Redemption Amounts determined in accordance with Condition 8(b) (*Optional Redemption*) (except that, in the case of Fixed Rate Bonds and Indexed Bonds for the purposes of this Condition 11(a), the "**Reference Date**" means the date two Business Days prior to the despatch of the notice of redemption given under this Condition 11(a)) or as specified in the applicable Final Terms.

(b) Confirmation of no Event of Default

The Issuer, pursuant to the terms of the Common Terms Agreement, shall provide written confirmation to the Bond Trustee, on an annual basis, that no Event of Default has occurred in relation to the Issuer.

(c) Enforcement of Security

If the Bond Trustee gives written notice to the Issuer and the Security Trustee that an Event of Default has occurred under the Bonds of any Sub-Class, a Standstill Period shall commence. The Security Trustee may only enforce the Security acting in accordance with the STID and, subject to certain limitations on

enforcement during a Standstill Period, on the instructions of the Majority Creditors.

(d) *Automatic Acceleration*

In the event of the acceleration of the Secured Liabilities (other than a Permitted Share Pledge Acceleration, a Permitted Hedge Termination or a Permitted Lease Termination (as defined in the Master Definitions Agreement) as set out in the STID), the Bonds of each Series shall automatically become due and repayable at their respective Redemption Amounts determined in accordance with Condition 8(b*) (Optional Redemption)* (except that, in the case of Fixed Rate Bonds and Indexed Bonds for the purposes of this Condition 11(d), **"Reference Date"** means the date two Business Days prior to the date of such acceleration) or as specified in the applicable Final Terms plus, in each case, accrued and unpaid interest thereon.

12 Enforcement Against Issuer

No Bondholder is entitled to take any action against the Issuer or, in the case of the holders of Wrapped Bonds, against the Financial Guarantor or against any assets of the Issuer or any Financial Guarantor to enforce its rights in respect of the Bonds or to enforce any of the Security or to enforce any Financial Guarantee unless the Bond Trustee or the Security Trustee (as applicable), having become bound so to proceed, fails or neglects to do so within a reasonable period and such failure or neglect is continuing. The Security Trustee will act (subject to Condition 11(c) *(Enforcement of Security))* on the instructions of the Majority Creditors pursuant to the STID, and neither the Bond Trustee nor the Security Trustee shall be bound to take any such action unless it is indemnified and/or secured to its satisfaction against all fees, costs, expenses, liabilities, claims and demands to which it may thereby become liable or which it may incur by so doing.

Neither the Bond Trustee nor the Bondholders may institute against, or join any person in instituting against, the Issuer any bankruptcy, winding up, re-organisation, arrangement, insolvency or liquidation proceeding (except for the appointment of a receiver and manager pursuant to the terms of the Security Agreement and subject to the STID) or other proceeding under any similar law for so long as any Bonds are outstanding or for two years and a day after the latest Maturity Date on which any Bond of any Series is due to mature.

13 Prescription

Claims against the Issuer for payment in respect of the Bonds, Receipts or Coupons (which, for this purpose, shall not include Talons) shall be prescribed and become void unless made within ten years (in the case of principal) or five years (in the case of interest) from the appropriate Relevant Date (as defined in Condition 6(i) (*Definitions*)) in respect thereof.

14 Replacement of Bonds, Coupons, Receipts and Talons

If any Bearer Bond, Registered Bond, Receipt, Coupon or Talon is lost, stolen, mutilated, defaced or destroyed it may be replaced, subject to applicable laws and requirements of the London Stock Exchange (in the case of listed Bonds) (and each other listing authority, stock exchange and or quotation system upon which the relevant Bonds have then been admitted to listing, trading and/or quotation), at the specified office of the Principal Paying Agent or, as the case may be, the Registrar upon payment by the claimant of the expenses incurred in connection with such replacement and on such terms as to evidence, security, indemnity and otherwise as the Issuer may require. Mutilated or defaced Bonds, Receipts, Coupons or Talons must be surrendered before replacements will be issued.

15 Meetings of Bondholders, Modification, Waiver and Substitution

(a) Decisions of Majority Creditors

The STID contains provisions dealing with the manner in which matters affecting the interests of the Secured Creditors (including the Bond Trustee and the Bondholders) will be dealt with, Bondholders will (subject to various Reserved Matters and Entrenched Rights) be bound by the decisions of the Majority Creditors (and additionally in a Default Situation (as defined in the Master Definitions Agreement) decisions made pursuant to the Emergency Instruction Procedure (as set out in Clause 9.12 of the STID)).

In the circumstances which do not relate to Entrenched Rights or Reserved Matters of the Bondholders (as set out in the STID), the Bond Trustee shall be entitled to vote as the DIG Representative (as defined in the Master Definitions Agreement) of holders of each Sub-Class of Wrapped Bonds (following the occurrence of an FG Event of Default (as defined in the Master Definitions Agreement) in respect of the Financial Guarantor of those Wrapped Bonds which is continuing) and of each Sub-Class of Unwrapped Bonds on intercreditor issues (“**Intercreditor Issues**”) but shall not be entitled to convene a meeting of any one or more Sub-Classes of Bondholders to consider the relevant matter unless a Default Situation is subsisting. If a Default Situation has occurred and is subsisting, the Bond Trustee may vote on Intercreditor Issues in its absolute discretion or shall vote in accordance with a direction by those holders of such outstanding Class A Bonds or, if there are no Class A Bonds outstanding, Class B Bonds (i) by means of an Extraordinary Resolution of the relevant Sub-Class of Bonds or (ii) (in respect of a DIG Proposal (as defined in the Master Definitions Agreement) to terminate a Standstill (as defined in the Master Definitions Agreement)) as requested in writing by the holders of at least one quarter of the Principal Amount Outstanding of the relevant Sub-Class of Class A Bonds then outstanding, or if there are no Class A Bonds outstanding, Class B Bonds. In any case, the Bond Trustee shall not be obliged to vote unless it has been indemnified and/or secured to its satisfaction.

Whilst a Default Situation is subsisting, certain decisions and instructions may be required in a timeframe which does not allow the Bond Trustee to convene Bondholder meetings. To cater for such circumstances, the STID provide for an emergency instruction procedure. The Security Trustee will be required to act upon instructions contained in an emergency notice (an "**Emergency Instruction Notice**"). An Emergency Instruction Notice must be signed by DIG Representatives (the "**EIN Signatories**") representing 66 ⅔ per cent. or more of the aggregate Outstanding Principal Amount (as defined in the Master Definitions Agreement) of the Qualifying Class A Debt or following repayment in full of the Class A Debt, the Qualifying Class B Debt after, *inter alia*, excluding the proportion of Qualifying Debt in respect of which the Bond Trustee is the DIG Representative and in respect of which the Bond Trustee has not voted. The Emergency Instruction Notice must specify the emergency action which the Security Trustee is being instructed to take and must certify that, unless such action is taken within the time frame specified in the Emergency Instruction Notice, the interests of the EIN Signatories will be materially prejudiced.

(b) Meetings of Bondholders

The Bond Trust Deed contains provisions for convening meetings of the Bondholders to consider any matter affecting their interests, including the modification of the Bonds, the Receipts, the Coupons or any of the provisions of the Bond Trust Deed (in the case of Class A Wrapped Bonds and Class B Wrapped Bonds), the Financial Guarantees and any other Finance Document to which the Bond Trustee is a party (subject to the terms of the STID)). Any modification may (except in relation to any Entrenched Right or Reserved Matter of the Bond Trustee (as set out in the STID) subject to the terms of the STID including, in the case of any of the Class A Wrapped Bonds or Class B Wrapped Bonds, to Entrenched Rights or Reserved Matters of any Financial Guarantor (as set out in the STID) and subject to the provisions concerning ratification and/or meetings of particular combinations of Sub-Classes of Bonds as set out in Condition 16(b) (*Exercise of rights by Bond Trustee*) and the Bond Trust Deed), be made if sanctioned by a resolution passed at a meeting of such Bondholders duly convened and held in accordance with the Bond Trust Deed by a majority of not less than three-quarters of the votes cast (an **"Extraordinary Resolution**") at such meeting. Such a meeting may be convened by the Bond Trustee or the Issuer, and shall be convened by the Issuer upon the request in writing of the relevant Bondholders holding not less than one-tenth in nominal amount of the relevant Bonds for the time being outstanding.

The quorum at any meeting convened to vote on an Extraordinary Resolution will be one or more persons holding or representing not less than 50 per cent. in nominal amount of the relevant Bonds for the time being outstanding or, at any adjourned meeting, one or more persons being or representing Bondholders, whatever the nominal amount of the relevant Bonds held or represented, provided however, that certain matters as set out in paragraph 5 of the Fourth Schedule to the Bond Trust Deed (the "**Basic Terms Modifications**") in respect of the holders

of any particular Sub-Class of Bonds may be sanctioned only by an Extraordinary Resolution passed at a meeting of Bondholders of the relevant Sub-Class of Bonds at which one or more persons holding or representing not less than three-quarters or, at any adjourned meeting, one-quarter in nominal amount of the outstanding Bonds form a quorum. Any Extraordinary Resolution duly passed at any such meeting shall be binding on all the relevant Bondholders, Receiptholders and Couponholders whether present or not.

In addition, a resolution in writing signed by or on behalf of all Bondholders who for the time being are entitled to receive notice of a meeting of Bondholders under the Bond Trust Deed will take effect as if it were an Extraordinary Resolution. Such a resolution in writing may be contained in one document or several documents in the same form, each signed by or on behalf of one or more Bondholders.

(c) *Modification, consent and waiver*

As more fully set out in the Bond Trust Deed (and subject to the conditions and qualifications therein), the Bond Trustee may, without the consent of the Bondholders of any Sub-Class, concur with the Issuer or any other relevant parties in making (i) any modification of these Conditions, the Bond Trust Deed, any Financial Guarantee or any Finance Document which is of a formal, minor or technical nature or is made to correct a manifest error; and (ii) (except as mentioned in the Bond Trust Deed and subject to the terms of the STID) any other modification and granting any consent under or waiver or authorisation of any breach or proposed breach of these Conditions, the Bond Trust Deed, such Financial Guarantee or any such Finance Document or other document which is, in the opinion of the Bond Trustee, not materially prejudicial to the interests of the Bondholders of that Sub-Class. Any such modification, consent, waiver or authorisation shall be binding on the Bondholders of that Sub-Class, and the holders of all relevant Receipts and Coupons and, if the Bond Trustee so requires, notice thereof shall be given by the Issuer to the Bondholders of that Sub-Class as soon as practicable thereafter.

The Bond Trustee shall be entitled to assume that any such modification, consent, waiver or authorisation is not materially prejudicial to the Bondholders if the Rating Agencies confirm that there will not be any adverse effect thereof on the original issue ratings of the Bonds.

(d) *Substitution of the Issuer*

As more fully set forth in the STID (and subject to the conditions and qualifications therein), the Bond Trustee may also agree with the Issuer, without reference to the Bondholders, to the substitution of another corporation in place of the Issuer as principal debtor in respect of the Bond Trust Deed and the Bonds of all Series and subject to the Class A Wrapped Bonds continuing to carry the unconditional guarantee of the relevant Financial Guarantor.

16 Bond Trustee Protections

(a) Trustee considerations

Subject to the terms of the STID and Condition 16(b) (*Exercise of rights by Bond Trustee*), in connection with the exercise, under these Conditions, the Bond Trust Deed, any Financial Guarantee or any Finance Document, of its rights, powers, trusts, authorities and discretions (including any modification, consent, waiver or authorisation), the Bond Trustee shall have regard to the interests of the holders of the relevant Series of Class A Bonds, or if there are no Class A Bonds outstanding, the Class B Bonds then outstanding provided that, if the Bond Trustee considers, in its sole opinion, that there is a conflict of interest between the holders of two or more Sub-Classes of Bonds of such Class, it shall consider the interests of the holders of the Sub-Class of Class A Bonds, or if there are no Class A Bonds outstanding, the Class B Bonds outstanding with the shortest dated maturity and will not have regard to the consequences of such exercise for the holders of other Sub-Classes of Bonds or for individual Bondholders, resulting from their being for any purpose domiciled or resident in, or otherwise connected with, or subject to the jurisdiction of, any particular territory. The Bond Trustee shall not be entitled to require from the Issuer or any Financial Guarantor, nor shall any Bondholders be entitled to claim from the Issuer, any Financial Guarantor or the Bond Trustee, any indemnification or other payment in respect of any consequence (including any tax consequence) for individual Bondholders of any such exercise.

(b) Exercise of rights by Bond Trustee

Except as otherwise provided in these Conditions and the Bond Trust Deed, when exercising any rights, powers, trusts, authorities and discretions relating to or contained in these Conditions or the Bond Trust Deed (other than in determining or in respect of any Entrenched Right or Reserved Matter relating to the Bonds or any other Basic Terms Modification), which affects or relates to any Class A Wrapped Bonds and/or Class B Wrapped Bonds, the Bond Trustee shall only act with the consent of the relevant Financial Guarantor(s) (provided no FG Event of Default has occurred and is continuing) in accordance with the provisions of the Bond Trust Deed and the Bond Trustee shall not be required to have regard to the interests of the Bondholders in relation to the exercise of such rights, powers, trusts, authorities and discretions and shall have no liability to any Bondholders as a consequence of so acting. As a consequence of being required to act only with the consent of the relevant Financial Guarantor(s) in the circumstances referred to in the previous sentence, the Bond Trustee may not, notwithstanding the provisions of these Conditions, be entitled to act on behalf of the holders of any Sub-Classes of Bonds. Subject as provided in these Conditions and the Bond Trust Deed, the Bond Trustee will exercise its rights under, or in relation to, the Bond Trust Deed, the Conditions or any Financial Guarantee in accordance with

the directions of the relevant Bondholders, but the Bond Trustee shall not be bound as against the Bondholders to take any such action unless it has (i) (a) (in respect of the matters set out in Condition 11 *(Events of Default)* and Condition 15(a) *(Decisions of the Majority Creditors)* only) been so requested in writing by the holders of at least 25 per cent. in nominal amount of the relevant Sub-Classes of Bonds outstanding or (b) been so directed by an Extraordinary Resolution and (ii) been indemnified and/or furnished with security to its satisfaction.

(c) *Decisions under STID binding on all Bondholders*

Subject to the provisions of the STID and the Entrenched Rights and Reserved Matters of the Bond Trustee and the Bondholders, decisions of the Majority Creditors and (in a Default Situation) decisions made pursuant to the Emergency Instructions Procedures will bind the Bond Trustee and the Bondholders in all circumstances.

17 Notices

Notices to holders of Registered Bonds will be posted to them at their respective addresses in the Register and deemed to have been given on the date of posting. Other notices to Bondholders will be valid if published in a leading daily newspaper having general circulation in London (which is expected to be the Financial Times). The Issuer shall also ensure that all notices are duly published in a manner which complies with the rules and regulations of the London Stock Exchange and any other listing authority, stock exchange and/or quotation system on which the Bonds are for the time being listed. Any such notice (other than to holders of Registered Bonds as specified above) shall be deemed to have been given on the date of such publication or, if published more than once or on different dates, on the first date on which publication is made. Couponholders and Receiptholders will be deemed for all purposes to have notice of the contents of any notice given to the holders of Bearer Bonds in accordance with this Condition 17.

So long as any Bonds are represented by Global Bonds, notices in respect of those Bonds may be given by delivery of the relevant notice to Euroclear Bank S.A./N.V. as operator of the Euroclear System or Clearstream Banking, *société anonyme* or any other relevant clearing system as specified in the relevant Final Terms for communication by them to entitled account holders in substitution for publication in a daily newspaper with general circulation in London. Such notices shall be deemed to have been received by the Bondholders on the day of delivery to such clearing systems.

18 Indemnification Of The Bond Trustee And Security Trustee

(a) *Indemnification of the Bond Trustee*

The Bond Trust Deed contains provisions for indemnification of the Bond Trustee, and for its relief from responsibility, including provisions relieving it from taking any action including taking proceedings against the Issuer, any Financial Guarantor and or any other person unless indemnified and/or secured to its satisfaction. The Bond Trustee or any of its affiliates (as defined in Condition 7

(*Indexation*)) are entitled to enter into business transactions with the Issuer, any Financial Guarantor, the other Secured Creditors or any of their respective subsidiaries or associated companies without accounting for any profit resulting therefrom.

(b) *Indemnification of the Security Trustee*

Subject to the Entrenched Rights and Reserved Matters of the Security Trustee, the Security Trustee will only be required to take any action under or in relation to, or to enforce or protect the Security, or any other security interest created by a Finance Document, or a document referred to therein, if instructed to act by the Majority Creditors or Secured Creditors (or their representatives) (as appropriate) and if indemnified to its satisfaction.

(c) *Directions, Duties and Liabilities*

Neither the Security Trustee nor the Bond Trustee, in the absence of its own wilful misconduct, gross negligence or fraud, and in all cases when acting as directed by or subject to the agreement of the Majority Creditors or Secured Creditors (or their representatives) (as appropriate), shall in any way be responsible for any loss, costs, damages or expenses or other liability, which may result from the exercise or non-exercise of any consent, waiver, power, trust, authority or discretion vested in the Security Trustee or the Bond Trustee pursuant to the STID, any Finance Document or any Ancillary Document (as defined in the Master Definitions Agreement).

19 European Economic and Monetary Union

(a) *Notice of redenomination*

The Issuer may, without the consent of the Bondholders, and on giving at least 30 days' prior notice to the Bondholders, the Financial Guarantors, the Bond Trustee and the Principal Paying Agent, designate a date (the "**Redenomination Date**"), being an Interest Payment Date under the Bonds falling on or after the date on which the United Kingdom becomes a Participating Member State.

(b) *Redenomination*

Notwithstanding the other provisions of these Conditions, with effect from the Redenomination Date:

(i) the Bonds of each Sub-Class denominated in sterling (the "**Sterling Bonds**") shall be deemed to be redenominated into Euro in the denomination of Euro 0.01 with a principal amount for each Bond equal to the principal amount of that Bond in sterling, converted into Euro t the rate for conversion of such currency into Euro established by the Council of the European Union pursuant to the Treaty establishing the European Union, as amended, (including compliance with rules relating to rounding

in accordance with European Community regulations), provided, however, that, if the Issuer determines, with the agreement of the Bond Trustee, that the then current market practice in respect of the redenomination into Euro 0.01 of internationally offered securities is different from that specified above, such provisions shall be deemed to be amended so as to comply with such market practice and the Issuer shall promptly notify the Bondholders, the London Stock Exchange and any stock exchange (if any) on which the Bonds are then listed and the Principal Paying Agent of such deemed amendments;

(ii) if Bonds have been issued in definitive form:

(a) all Bonds denominated in sterling will become void with effect from the date (the "Euro Exchange Date") on which the Issuer gives notice (the "Euro Exchange Notice") to the Bondholders and the Bond Trustee that replacement Bonds denominated in Euro are available for exchange (provided that such Bonds are available) and no payments will be made in respect thereof;

(b) the payment obligations contained in all Bonds denominated in sterling will become void on the Euro Exchange Date but all other obligations of the Issuer thereunder (including the obligation to exchange such Bonds in accordance with this Condition 19) shall remain in full force and effect; and

(c) new Bonds denominated in Euro will be issued in exchange for Sterling Bonds in such manner as the Principal Paying Agent or the Registrar, as the case may be, may specify and as shall be notified to the Bondholders in the Euro Exchange Notice;

(iii) all payments in respect of the Sterling Bonds (other than, unless the Redenomination Date is on or after such date as sterling ceases to be a sub-division of the Euro, payments of interest in respect of periods commencing before the Redenomination Date) will be made solely in Euro by cheque drawn on, or by credit or transfer to a Euro account (or any other account to which Euro may be credited or transferred) maintained by the payee with, a bank in the principal financial centre of any Participating Member State; and

(iv) a Bond may only be presented for payment on a day which is a business day in the place of presentation.

(c) Interest

Following redenomination of the Bonds pursuant to this Condition 19:

(i) where Sterling Bonds have been issued in definitive form, the amount of interest due in respect of the Sterling Bonds will be calculated by

reference to the aggregate principal amount of the Sterling Bonds presented for payment by the relevant holder and the amount of such payment shall be rounded down to the nearest Euro 0.01; and

(ii) the amount of interest payable in respect of each Sub-Class of Sterling Bonds for any Interest Period shall be calculated by applying the Interest Rate applicable to the Sub-Class of Bonds denominated in Euro ranking pari passu to the relevant Sub-Class.

20 Miscellaneous

(a) Governing Law

The Bond Trust Deed, STID, the Security Agreement, the Bonds, the Coupons, the Receipts, the Talons (if any), the relevant Financial Guarantee (if any) and the other Finance Documents are, and all matters arising from or in connection with such documents shall be governed by, and shall be construed in accordance with, English law.

(b) Jurisdiction

The courts of England are to have exclusive jurisdiction to settle any dispute that may arise out of or in connection with the Bonds, the Coupons, the Receipts, the Talons, the relevant Financial Guarantee (if any) and the Finance Documents and accordingly any legal action or proceedings arising out of or in connection with the Bonds, the Coupons, the Receipts, the Talons (if any) the relevant Financial Guarantee (if any) and/or the Finance Document may be brought in such courts. The Issuer has in each of the Finance Documents irrevocably submitted to the jurisdiction of such courts.

(c) Third Party Rights

No person shall have any right to enforce any term or condition of the Bonds or the Bond Trust Deed under the Contracts (Rights of Third Parties) Act 1999.

Forms of the Bonds

Form and Exchange - Bearer Bonds

Each Sub-Class of Bonds initially issued in bearer form will be issued either as a temporary global bond (the "**Temporary Global Bond**"), without Receipts, Coupons or Talons attached, or a permanent global bond (the "**Permanent Global Bond**"), without Receipts, Coupons or Talons attached, in each case as specified in the relevant Final Terms. Each Temporary Global Bond or, as the case may be, Permanent Global Bond (each a "**Global Bond**") will be delivered on or prior to the issue date of the relevant Sub-Class of the Bonds to a depositary or a common depositary for Euroclear and/or Clearstream, Luxembourg and/or

any other relevant clearing system on or about the Issue Date of the relevant Sub-Class.

The relevant Final Terms will also specify whether United States Treasury Regulation §1.163-5(c)(2)(i)(C) (the "**TEFRA C Rules**") or United States Treasury Regulation §1.163-5(c)(2)(i)(D) (the "**TEFRA D Rules**") are applicable in relation to the Bonds.

Temporary Global Bond exchangeable for Permanent Global Bond

If the relevant Final Terms specify the form of Bonds as being represented by **"**Temporary Global Bond exchangeable for a Permanent Global Bond**",** then the Bonds will initially be in the form of a Temporary Global Bond which will be exchangeable, in whole or in part, for interests in a Permanent Global Bond, without Receipts, Coupons or Talons attached, not earlier than 40 days after the Issue Date of the relevant Sub-Class of the Bonds upon certification as to non-U.S. beneficial ownership. No payments will be made under the Temporary Global Bond unless exchange for interests in the Permanent Global Bond is improperly withheld or refused. In addition, payments of interest in respect of the Bonds cannot be collected without such certification of non-U.S. beneficial ownership.

Whenever any interest in the Temporary Global Bond is to be exchanged for an interest in a Permanent Global Bond, the Issuer shall procure (in the case of first exchange) the prompt delivery (free of charge to the bearer) of such Permanent Global Bond, duly authenticated, to the bearer of the Temporary Global Bond or (in the case of any subsequent exchange) an increase in the principal amount of the Permanent Global Bond in accordance with its terms against:

- presentation and (in the case of final exchange) surrender of the Temporary Global Bond at the specified office of the Paying Agent; and
- receipt by the Paying Agent of a certificate or certificates of non-U.S. beneficial ownership issued by Euroclear and/or Clearstream, Luxembourg and/or any other relevant clearing system,

within seven days of the bearer requesting such exchange.

The principal amount of the Permanent Global Bond shall be equal to the aggregate of the principal amounts specified in the certificates of non-U.S beneficial ownership; provided, however, that in no circumstances shall the principal amount of the Permanent Global Bond exceed the aggregate initial principal amount of the Temporary Global Bond and any Temporary Global Bond representing a fungible Sub-Class of Bonds with the Sub-Class of Bonds represented by the first Temporary Global Bond.

The Permanent Global Bond will be exchangeable in whole, but not in part, for Bonds in definitive form ("**Definitive Bonds**"):

- on the expiry of such period of notice as may be specified in the relevant Final Terms; or
- at any time, if so specified in the relevant Final Terms; or
- if the relevant Final Terms specify "in the limited circumstances described in the Permanent Global Bond", then if (a) Euroclear or Clearstream, Luxembourg or any other relevant clearing system is closed for business for a continuous period of 14 days (other than by reason of legal holidays) or announces an intention permanently to cease business or (b) any of the circumstances described in Condition 11(a) (*Events of Default*) occurs; or
- the Issuer certifies to the Bond Trustee that it has or will, on the next payment date for interest or principal, become subject to adverse tax consequences which would not be suffered if the Bonds are not represented by a Permanent Global Bond.

Whenever the Permanent Global Bond is to be exchanged for Definitive Bonds, the Issuer shall procure the prompt delivery (free of charge to the bearer) of such Definitive Bonds, duly authenticated and with Receipts, Coupons and Talons attached (if so specified in the relevant Final Terms), in an aggregate principal amount equal to the principal amount of the Permanent Global Bond to the bearer of the Permanent Global Bond against the surrender of the Permanent Global Bond at the Specified Office of the Paying Agent within 30 days of the bearer requesting such exchange but not earlier than 40 days after the Issue Date of such Bonds.

Temporary Global Bond exchangeable for Definitive Bonds

If the relevant Final Terms specifies the form of Bonds as being "Temporary Global Bond exchangeable for Definitive Bonds" and also specifies that the TEFRA C Rules are applicable or that neither the TEFRA C Rules nor the TEFRA D Rules are applicable, then the Bonds will initially be in the form of a Temporary Global Bond which will be exchangeable, in whole but not in part, for Definitive Bonds not earlier than 40 days after the Issue Date of the relevant Sub-Class of the Bonds.

If the relevant Final Terms specifies the form of Bonds as being "Temporary Global Bond exchangeable for Definitive Bonds" and also specifies that the TEFRA D Rules are applicable, then the Bonds will initially be in the form of a Temporary Global Bond which will be exchangeable, in whole or in part, for Definitive Bonds not earlier than 40 days after the Issue Date of the relevant Sub-Class of the Bonds upon certification as to non-U.S. beneficial ownership. Interest payments in respect of the Bonds cannot be collected without such certification of non-U.S. beneficial ownership.

Whenever the Temporary Global Bond is to be exchanged for Definitive Bonds, the Issuer shall procure the prompt delivery (free of charge to the bearer) of such Definitive Bonds, duly authenticated and with Receipts, Coupons and Talons attached (if so specified in the relevant Final Terms), in an aggregate principal amount equal to the principal amount of the Temporary Global Bond so exchanged to the bearer of the Temporary Global Bond against the presentation (and in the case of final exchange, surrender) of the Temporary Global Bond at the Specified Office of the Paying Agent within 30 days of the bearer requesting such exchange but not earlier than 40 days after the issue of such Bonds.

Permanent Global Bond exchangeable for Definitive Bonds

If the relevant Final Terms specifies the form of Bonds as being "Permanent Global Bond exchangeable for Definitive Bonds", then the Bonds will initially be in the form of a Permanent Global Bond which will be exchangeable in whole, but not in part, for Definitive Bonds:

- on the expiry of such period of notice as may be specified in the relevant Final Terms; or
- at any time, if so specified in the relevant Final Terms; or
- if the relevant Final Terms specifies "in the limited circumstances described in the Permanent Global Bond", then if (a) Euroclear or Clearstream, Luxembourg or any other relevant clearing system is closed for business for a continuous period of 14 days (other than by reason of legal holidays) or announces an intention permanently to cease business or (b) any of the circumstances described in Condition 11 (a) *(Events of Default)* occurs; or
- the Issuer certifies to the Bond Trustee that it has or will, on the next payment date for interest or principal, become subject to adverse tax consequences which would not be suffered if the Bonds are not represented by a Permanent Global Bond.

Whenever the Permanent Global Bond is to be exchanged for Definitive Bonds, the Issuer shall procure the prompt delivery (free of charge to the bearer) of such Definitive Bonds, duly authenticated and with Receipts, Coupons and Talons attached (if so specified in the relevant Final Terms), in an aggregate principal amount equal to the principal amount of the Permanent Global Bond to the bearer of the Permanent Global Bond against the surrender of the Permanent Global Bond at the Specified Office of the Paying Agent within 30 days of the bearer requesting such exchange but not earlier than 40 days after the Issue Date of such Bonds.

In the event that a Global Bond is exchanged for Definitive Bonds, such Definitive Bonds shall be issued in Specified Denominations(s) only. Bondholders who hold

Bonds in the relevant clearing system in amounts that are not integral multiples of a Specified Denomination may need to purchase or sell, on or before the relevant date of exchange, a principal amount of Bonds such that their holding is an integral multiple of a Specified Denomination.

Conditions applicable to the Bonds

The Conditions applicable to any Definitive Bond will be endorsed on that Bond and will consist of the Conditions set out under **"**Terms and Conditions of the Bonds**"** above and the provisions of the relevant Final Terms which supplement, amend, vary and/or replace those Conditions.

The Conditions applicable to any Global Bond will differ from those Conditions which would apply to the Definitive Bond to the extent described under "Provisions Relating to the Global Bonds".

Legend concerning United States persons

Global Bonds and Definitive Bonds having a maturity of more than 365 days and any Receipts, Coupons and Talons appertaining thereto will bear a legend to the following effect:

"Any United States person who holds this obligation will be subject to limitations under the United States income tax laws, including the limitations provided in Sections 165(j) and 1287(a) of the Internal Revenue Code."

The sections referred to in such legend provide that a United States person who holds a Bond, Receipt, Coupon or Talon will generally not be allowed to deduct any loss realised on the sale, exchange or redemption of such Bond, Receipt, Coupon or Talon and any gain (which might otherwise be characterised as capital gain) recognised on such sale, exchange or redemption will be treated as ordinary income. *Form and Exchange - Global Bond Certificates*

Global Certificates

Registered Bonds held in Euroclear and/or Clearstream, Luxembourg and/or other clearing system will be represented by a global bond certificate (each a "**Global Bond Certificate**") which will be registered in the name of a nominee for, and deposited with, a depositary for Euroclear and/or Clearstream, Luxembourg and/or such other relevant clearing system on or about the Issue Date of the relevant Sub-Class.

Exchange

The Global Bond Certificate will become exchangeable in whole, but not in part, for individual bond certificates (each an "**Individual Bond Certificate**") if (a) Euroclear or Clearstream, Luxembourg and/or other relevant clearing system is closed for business for a continuous period of 14 days (other than by reason of

legal holidays) or announces an intention permanently to cease business, (b) any of the circumstances described in Condition 11(a) (*Events of Default*) occurs, (c) at any time at the request of the registered Holder if so specified in the Final Terms or (d) the Issuer certifies to the Bond Trustee that it has or will, on the next payment date for interest or principal, become subject to adverse tax consequences which would not be suffered if the Bonds are not represented by a Global Bond Certificate.

Whenever the Global Bond Certificate is to be exchanged for Individual Bond Certificates, such will be issued in an aggregate principal amount equal to the principal amount of the Global Bond Certificate within seven business days of the delivery, by or on behalf of the registered Holder of the Global Bond Certificate to the Registrar or the Transfer Agents (as the case may be) of such information as is required to complete and deliver such Individual Bond Certificates (including the names and addresses of the persons in whose names the Individual Bond Certificates are to be registered and the principal amount of each such person's holding) against the surrender of the Global Bond Certificate at the specified office of the Registrar or the Transfer Agent (as the case may be). Such exchange will be effected in accordance with the provisions of the Agency Agreement and the regulations concerning the transfer and registration of Bonds scheduled thereto and, in particular, shall be effected without charge to any holder, but against such indemnity as the Registrar or the Transfer Agents (as the case may be) may require in respect of any tax or other duty of whatsoever nature which may be levied or imposed in connection with such exchange.

Rights Against Issuer

Under the Bond Trust Deed, persons shown in the records of Euroclear and/or Clearstream, Luxembourg and/or any other relevant clearing system as being entitled to interests in the Bonds will (subject to the terms of the Bond Trust Deed and the STID) acquire directly against the Issuer all those rights to which they would have been entitled if, immediately before the Global Bond or Global Bond Certificate became void, they had been the registered Holders of Bonds in an aggregate principal amount equal to the principal amount of Bonds they were shown as holding in the records of Euroclear, Clearstream, Luxembourg or any other relevant clearing system (as the case may be).

Provisions Relating To The Bonds While in Global Form

Clearing System Accountholders

References in the Conditions of the Bonds to "**Bondholder**" are references to the bearer of the relevant Global Bond or the person shown in the records of the relevant clearing system as the holder of the Global Bond Certificate.

Each of the persons shown in the records of Euroclear and/or Clearstream, Luxembourg and/or any other relevant clearing system, as the case may be, as

being entitled to an interest in a Global Bond or a Global Bond Certificate (each an "**Accountholder**") must look solely to Euroclear and/or Clearstream, Luxembourg and/or such other relevant clearing system (as the case may be) for such Accountholder's share of each payment made by the Issuer or, in the case of Wrapped Bonds, the relevant Financial Guarantor, to such Accountholder and in relation to all other rights arising under the Global Bond or Global Bond Certificate. The extent to which, and the manner in which, Accountholders may exercise any rights arising under a Global Bond or Global Bond Certificate will be determined by the respective rules and procedures of Euroclear and Clearstream, Luxembourg and any other relevant clearing system (as the case may be) from time to time. For so long as the relevant Bonds are represented by a Global Bond or Global Bond Certificate, Accountholders shall have no claim directly against the Issuer or, in the case of Wrapped Bonds, the relevant Financial Guarantor in respect of payments due under the Bonds and such obligations of the Issuer and, in the case of Wrapped Bonds, the relevant Financial Guarantor will be discharged by payment to the bearer of the Global Bond or the registered holder of the Global Bond Certificate, as the case may be.

Amendment to Conditions

Global Bonds will contain provisions that apply to the Bonds which they represent, some of which modify the effect of the Conditions of the Bonds as set out in this Prospectus. The following is a summary of certain of those provisions:

*Meetings: The holder of a Global Bond or Global Bond Certificate shall be treated as being two persons for the purposes of any quorum requirements of a meeting of Bondholders and, at any such meeting, the holder of a Global Bond or Global Bond Certificate shall be treated as having one vote in respect of each minimum denomination of Bonds for which such Global Bond or Global Bond Certificate may be exchanged.

*Cancellation: Cancellation of any Bond represented by a Global Bond or Global Bond Certificate that is required by the Conditions to be cancelled (other than upon its redemption) will be effected by reduction in the principal amount of the relevant Global Bond or Global Bond Certificate.

*Notices: So long as any Bonds are represented by a Global Bond or Global Bond Certificate and such Global Bond or Global Bond Certificate is held on behalf of Euroclear, Clearstream, Luxembourg or any other relevant Clearing System, notices to the Bondholders may be given, subject always to listing requirements, by delivery of the relevant notice to Euroclear, Clearstream, Luxembourg or any other relevant Clearing System for communication by it to entitled Accountholders in substitution for publication as provided in the Conditions.

PRO FORMA FINAL TERMS

Set out below is the form of Final Terms which will be completed for each Tranche of Bonds issued under the Programme.

Final Terms dated [●]

SOUTHERN WATER SERVICES (FINANCE) LIMITED

Issue of [Sub-Class [-[●] (delete as appropriate)] [Aggregate Nominal Amount of Sub-Class]
[Title of Bonds]
[(if Class A Wrapped Bonds or Class B Wrapped Bonds issued including the following:):
unconditionally and irrevocably guaranteed as to scheduled payments of principal and interest

by

[**Name of Financial Guarantor**]]
under the £6,000,000,000 Guaranteed Bond Programme

PART A – CONTRACTUAL TERMS

Terms used herein shall be deemed to be defined as such for the purposes of the conditions set forth in the Prospectus dated [●] [and the supplemental Prospectus dated [●] which [together] constitute[s] (i) a base prospectus for the purposes of the Prospectus Directive (Directive 2003/71/EC) (the "**Prospectus Directive**") and (ii) listing particulars for the purposes of Listing Rule 2.2.11 of the Listing Rules of the Financial Services Authority (the "**Listing Rules**"). This document constitutes the Final Terms of the Bonds described herein for the purposes of [Article 5.4 of the Prospectus Directive] [Listing Rule 4.2.3 of the Listing Rules] and must be read in conjunction with such Prospectus [as so supplemented]. Full information on the Issuer and the offer of the Bonds is only available on the basis of the combination of these Final Terms and the Prospectus. [The Prospectus [and the supplemental Prospectus] [is] [are] available for viewing at [●].]

[*The following alternative language applies if the first tranche of an issue which is being increased was issued under a Prospectus with an earlier date.*]

[Terms used herein shall be deemed to be defined as such for the purposes of the Conditions (the "**Conditions**") set forth in the Prospectus dated [original date] [and the supplemental Prospectus dated [●]. This document constitutes the Final Terms of the Bonds described herein for the purposes of [Article 5.4 of the Prospectus Directive (Directive 2003/71/EC) (the "**Prospectus Directive**")][1] [and Listing Rule 4.2.3 of the Listing Rules of the Financial Services Authority (the "**Listing Rules**")][2] and must be read in conjunction with the Prospectus dated [current date] [and the supplemental Prospectus dated [●], which [together] constitute[s] a base prospectus for

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[1] Delete wording in square brackets if the Bonds are to be listed on the London Stock Exchange's Professional Securities Market.

[2] Delete wording in square brackets if the Bonds are to be listed on the London Stock Exchange's Gilt-Edged and Fixed Interest Market.

the purposes of the Prospectus Directive and (ii) listing particulars for the purposes of Listing Rule 2.2.11 of the Listing Rules, save in respect of the Conditions which are extracted from the Prospectus dated [original date] [and the supplemental Prospectus dated [●]] and are attached hereto. Full information on the Issuer and the offer of the Bonds is only available on the basis of the combination of these Final Terms and the Prospectuses dated [original date] and [current date] [and the supplemental Prospectuses dated [●] and [●]. [The Prospectuses [and the supplemental Prospectuses] are available for viewing at [●].]

[Repayment of the principal and payment of any interest or premium in connection with the Bonds has not been guaranteed by the Financial Guarantor (as referred to below) or by any other financial institution.]

[*Note: include above paragraph if neither Class A Wrapped Bonds nor Class B Wrapped Bonds being described in the Final Terms.*]

[*When completing Final Terms or adding any other final terms or information consideration should be given as to whether such terms or information constitute (i) (in the case of an application to list the Bonds on the London Stock Exchange's Gilt-Edged and Fixed Interest Market) "significant new factors" and consequently trigger the need for a supplement to the Prospectus under Article 16 of the Prospectus Directive or (ii) (in the case of an application to list the Bonds on the London Stock Exchange's Professional Securities Market) "a significant change" and consequently trigger the need for a supplement to the Prospectus under section 81 of the FSMA.*]

[*Include whichever of the following apply or specify as "Not Applicable" (N/A). Note that the numbering should remain as set out below, even if "Not Applicable" is indicated for individual paragraphs or sub-paragraphs. Italics denote directions for completing the Final Terms.*]

1	(i)	Issuer	Southern Water Services (Finance) Limited
	(ii)	Guarantors:	Southern Water Services Limited, SWS Holdings Limited and SWS Group Holdings Limited
	(iii)	Financial Guarantor:	[Name of Financial Guarantor] [*delete if not Wrapped Bonds*]
2	(iii)	Series Number	[●]
	(iv)	Sub-Class Number: (*If fungible with an existing Sub-Class, details of that Sub-Class, including the date on which the Bonds become fungible.*)	[●]
3	Relevant Currency or Currencies:		[●]

4	Aggregate Nominal Amount of Bonds admitted to trading:		
	(i)	Series:	[●]
	(ii)	Tranche:	[●]
	(iii)	Sub-Class:	[●]
5	(i)	Issue Price:	[●] per cent. of the Aggregate Nominal Amount [plus accrued interest from [*insert date*]] (*in the case of fungible issues only, if applicable*)]
	(ii)	Net proceeds: (required only for listed issues)	[●]
6	Specified Denominations:		[●]
	(*To avoid certain on-going reporting obligations under the Transparency Directive and to fall within the wholesale debt securities regime, the minimum denomination should be Euro 50,000 or equivalent if Bonds to be listed on an EU regulated market. In the case of Registered Bonds, this means the minimum integral amount in which transfers can be made). Bonds (including Bonds denominated in Sterling) in respect of which the issue proceeds are to be accepted by the Issuer in the United Kingdom or whose issue otherwise constitutes a contravention of section 19 FSMA and which have a maturity of less than one year must have a minimum redemption value of £100,000 (or its equivalent in other currencies).*)		
	"Tradeable Amount":		[●]
7	(i)	Issue Date:	[●]
	(ii)	Interest Commencement Date (if different from the Issue Date):	[●]
8	Maturity Date:		[*specify date or (for Floating Rate Bonds) Interest Payment Date falling in [the relevant month and year*]]
9	Instalment Date:		[Not Applicable/*specify*]

10	Interest Basis:	[[●] per cent. Fixed Rate] [[specify reference] +/- [●] per cent. Floating Rate] [Zero Coupon] [Index Linked Interest] [specify other]
11	Redemption/Payment Basis:	[Redemption at par] [Index Linked Redemption] [Partly Paid] [Instalment] [Dual Currency] [specify other]
12	Change of Interest or Redemption/Payment Basis:	[*Specify details of any provision for convertibility of Bonds into another interest or redemption/payment basis*]
13	Call Options:	Issuer Call Option [(*further particulars specified below*)]
14	(i) Status and Ranking:	[*if Class A Wrapped Bonds or Class A Unwrapped Bonds*] The Class A Wrapped Bonds and Class A Unwrapped Bonds rank *pari passu* among each other in terms of interest and principal payments and rank in priority to the Class B Bonds. [*if Class B Bonds:*] The Class B Wrapped Bonds and the Class B Unwrapped Bonds rank *pari passu* among each other and are subordinated in terms of interest and principal payments to the Class A Bonds.
	(ii) Status of the Guarantees:	Senior
	(iii) Status of the Financial Guarantee:	The Financial Guarantee will rank *pari passu* with all unsecured obligations of the Financial Guarantor. [*Only required if Wrapped Bonds. Specify for Financial Guarantor*]

A12.5.1.2

	(iv) FG Event of Default (if not MBIA)	
	[v] [Date [Board] approval for issuance of Bonds obtained:	[●] and [●] respectively]] (*N.B. Only relevant where Board (or similar) authorisation is required for the particular tranche of Bonds*)
15	Method of distribution:	[Syndicated/Non-syndicated]

PROVISIONS RELATING TO INTEREST (IF ANY) PAYABLE

16	Fixed Rate Bond Provisions:	[Applicable/Not Applicable] (*If not applicable, delete the remaining sub-paragraphs of this paragraph*)
	(i) Interest Rate:	[●] per cent. per annum [payable [annually/semi-annually/quarterly/monthly] in arrear]
	(ii) Interest Determination Date:	[●] in each year (*insert regular interest payment dates, ignoring issue date or maturity date in the case of a long or short first or last coupon - only relevant where day count fraction is Actual/Actual (ICMA)*)
	(iii) Interest Payment Date(s):	[●] in each year [adjusted in accordance with [*specify Business Day Convention and applicable Business Centre(s)for the definition of "Business Day"*]/not adjusted]
	(iv) First Interest Payment Date	[●]
	(v) Fixed Coupon Amount[(s)]:	[●] per [●] in Nominal Amount
	(vi) Broken Amount(s):	[*Insert particulars of any initial or final broken interest amounts which do not correspond with the Fixed Coupon Amount[(s)]*]
	(vii) Day Count Fraction:	[Actual/Actual ICMA] [Actual/365 or Actual/Actual] [Actual/365 Fixed] [Actual/360] [30/360 or 360/360 or bond basis] [30E/360 or Eurobond Basis]
	(viii) Other terms relating to the method of calculating interest for Fixed Rate Bonds:	[*Not Applicable/give details*]
	(ix) Reference Gilt	[●]

17	Floating Rate Bond Provisions:		[Applicable/Not Applicable] (*If not applicable, delete the remaining sub-paragraphs of this paragraph*)
	(i)	Specified Period(s)/Specified Interest Payment Dates:	[●]
	(ii)	First Interest Payment Date	[●]
	(iii)	Business Day Convention:	[Following Business Day Convention/Modified Following Business Day Convention/Preceding Business Day Convention/other (*give details*)]
	(iv)	Manner in which the Rate(s) of Interest is/are to be determined:	[Screen Rate Determination/ISDA Determination/other (*give details*)]
	(v)	Party responsible for calculating the Rate(s) of Interest, Interest Amount(s) and Redemption Amount (if not the Agent Bank):	[Not Applicable/Calculation Agent]
	(vi)	Screen Rate Determination:	
		– Relevant Rate:	[●]
		–Interest Determination Date(s):	[●]
		–Page:	[●]
		–Relevant Time:	[*local time when Relevant Rate set*]
	(vii)	ISDA Determination:	
		– Floating Rate Option:	[●]
		– Designated Maturity:	[●]
		– Specified Duration:	[*if other than the relevant Interest Period*]
		– Reset Date:	[●]
	(viii)	Margin(s):	[+/-][●] per cent. per annum
	(ix)	Minimum Rate of Interest:	[Not Applicable]
	(x)	Maximum Rate of Interest:	[Not Applicable]
	(xi)	Day Count Fraction:	[Actual/Actual ICMA] [Actual/365 or Actual/Actual] [Actual/365 Fixed] [Actual/360] [30/360 or 360/360 or Bond Basis] [30E/360 or Eurobond Basis]
	(xii)	Additional Business Centre(s):	[●]

	(xiii)	Fall back provisions, rounding provisions, denominator and any other terms relating to the method of calculating interest on Floating Rate Bonds, if different from those set out in the Conditions:	[●]
	(xiv)	Relevant Financial Centre:	[●]
	(xv)	Representative Amount:	[●]
	(xvi)	Reference Banks:	[*if none specified, four major banks selected by Agent Bank/Calculation Agent*]
18	Zero Coupon Bond Provisions:		[Applicable/Not Applicable]
			(*If not applicable, delete the remaining subparagraphs of this paragraph*)
	(i)	Accrual Yield:	[●] per cent. per annum
	(ii)	Reference Price:	[●]
	(iii)	Any other formula/basis of determining amount payable:	[●]
	(iv)	Day Count Fraction in relation to Early Redemption Amounts and late payment:	[Condition 8(e)/specify other]
			(*Consider applicable day count fraction if not U.S. dollar denominated*)
19	Indexed Bond Provisions:		[Applicable/Not Applicable]
			(*If not applicable, delete the remaining subparagraphs of this paragraph*)
	(i)	Index/Formula:	[UK Retail Price Index]
	(ii)	Interest Rate:	[●]
	(iii)	Party responsible for calculating the Rate(s) of Interest, Interest Amount and Redemption Amount(s) (if not the Agent Bank):	[Not Applicable/Calculation Agent]
	(iv)	Provisions for determining Coupon where calculation by reference to Index and/or Formula is impossible or impracticable:	Applicable – Condition 7(c) and 7(e)
	(v)	Interest Payment Dates:	[●]
	(vi)	First Interest Payment Date:	[●]

	(vii)	Business Day Convention:	[Following Business Day Convention/Modified Following Business Day Convention/Preceding Business Day Convention/other (*give details*)]
	(viii)	Minimum Indexation Factor:	[Not Applicable/*specify*]
	(ix)	Maximum Indexation Factor:	[Not Applicable/*specify*]
	(x)	Limited Indexation Month(s):	[●]
	(xi)	Reference Gilt	[●]
	(xii)	Day Count Fraction:	[Actual/Actual ICMA] [Actual/365 or Actual/Actual] [Actual/365 Fixed] [Actual/360] [30/360 or 360/360 or Bond Basis] [30E/360 or Eurobond Basis]
20	Dual Currency Bond Provisions		[Applicable/Not Applicable] [*If not applicable, delete the remaining sub-paragraphs of this paragraph*]
	(i)	Rate of Exchange/method of calculating Rate of Exchange:	[Give details]
	(ii)	Party responsible for calculating the Rate(s) of Interest, Interest Amount and Redemption Amount(s) (if not the Agent Bank):	[Not Applicable/Calculation Agent]
	(iii)	Provisions applicable where calculation by reference to Rate of Exchange impossible or impracticable:	[●]
	(iv)	Person at whose option Specified Currency(ies) is/are payable:	[●]

PROVISIONS RELATING TO REDEMPTION

21	Issuer Call Option:		Applicable in accordance with Condition 8(b)/Not Applicable (*If not applicable, delete the remaining sub-paragraphs of this paragraph*)
	(i)	Optional Redemption Date(s):	Any Interest Payment Date [falling on or after [●] and at a premium of [●] (*delete for non-Floating Rate Bonds*).]
	(ii)	Optional Redemption Amount(s) and method, if any, of calculation of such amount(s):	[●]

	(iii)	If redeemable in part:	
		Minimum Redemption Amount:	[Not Applicable]
		Maximum Redemption Amount:	[Not Applicable]
	(iv)	Notice period (if other than as set out in the Conditions):	[Not Applicable]
22	Final Redemption Amount:		[Principal Amount Outstanding plus accrued but unpaid interest]

GENERAL PROVISIONS APPLICABLE TO THE BONDS

23	Form of Bonds		[Bearer/Registered]
	(i)	If issued in Bearer form:	[Temporary Global Bond exchangeable for a Permanent Global Bond which is exchangeable for Definitive Bonds on [●] days' notice/at any time/in the limited circumstances specified in the Permanent Global Bond/for tax reasons.] [Temporary Global Bond exchangeable for Definitive Bonds on [●] days' notice.] (Permanent Global Bond exchangeable for Definitive Bonds on [●] days' notice/at any time/in the limited circumstances specified in the Permanent Global Bond/for tax reasons.)
	(ii)	If Registered Bonds:	[Global Bond Certificate exchangeable for Individual Bond Certificates]
24	Relevant Financial Centre(s) or other special provisions relating to Payment Dates:		[Not Applicable/give details.]
25	Talons for future Coupons or Receipts to be attached to Definitive Bonds (and dates on which such Talons mature):		[Yes/No. *If yes, give details*]
26	Details relating to Partly Paid Bonds: amount of each payment comprising the Issue Price and date on which each payment is to be made and consequences (if any) of failure to pay, including any right of the Issuer to forfeit the Bonds and interest due on late payment:		[Not Applicable/*give details*]

27	Details relating to Instalment Bonds:	[Not Applicable/*give details*]
	(i) Instalment Date:	[●]
	(ii) Instalment Amount:	[●]
28	Redenomination, renominalisation and reconventioning provisions:	[Not Applicable/The provisions [in Condition 19/annexed to this Final Terms] apply]
29	Consolidation provisions:	[Not Applicable/The provisions annexed to this Final Terms] apply]
30	Other final terms:	[Not Applicable/*give details*]
		(*When adding any other final terms consideration should be given as to whether such terms constitute a "significant new factor" and consequently trigger the need for a supplement to the Prospectus under Article 16 of the Prospectus Directive.*)
31	TEFRA rules:	[TEFRA C/TEFRA D/Not Applicable]

ISSUER/SWS LOAN TERMS

32	Interest rate on relevant Term Advance/Index Linked Advances:	[●]
33	Term of relevant Term Advance/Index Linked Advances:	[●]
34	Other relevant provisions:	[●]

DISTRIBUTION

35	(i) If syndicated, names of Managers:	[Not Applicable/*give names*]
	(ii) Stabilising Manager (if any):	[Not Applicable/*give name*]
36	If non-syndicated, name of Dealer:	[Not Applicable/*give name*]
37	Additional selling restrictions:	[Not Applicable/*give details*]

LISTING AND ADMISSION TO TRADING APPLICATION

These Final Terms comprise the final terms required to list and have admitted to trading the issue of Bonds described herein pursuant to the listing of the Programme for the issuance of up to £3,000,000,000 Guaranteed Wrapped Bonds and £3,000,000,000 Guaranteed Unwrapped Bonds financing Southern Water Services Limited.

RESPONSIBILITY

The Issuer and each Guarantor accepts responsibility for the information contained in these Final Terms.

[The Financial Guarantor accepts responsibility for the [Financial Guarantor] Information contained in these Final Terms.]*

Signed on behalf of the Issuer:

By:...

Duly authorised

Signed on behalf of Southern Water Services Limited:

By:...

Duly authorised

Signed on behalf of SWS Holdings Limited:

By:...

Duly authorised

Signed on behalf of SWS Group Holdings Limited:

By:...

Duly authorised

[Signed on behalf of [Financial Guarantor]]

By:...

Duly authorised

* Delete as applicable

PART B – OTHER INFORMATION

1 Listing

(i) Listing:	[London/Luxembourg/other (*specify*)/None]
(ii)Admission to trading:	[Application has been made for the Bonds to be admitted to trading on [●] with effect from [●]. [Not Applicable.]
(iii) Estimate of total expenses related to admission to trading:	[●]

2 Ratings

Ratings:	The Bonds to be issued have been rated: [S&P: [●]] [Moody's: [●]] [Fitch: [●]] *(The above disclosure should reflect the rating allocated to Bonds of the type being issued under the Programme generally or, where the issue has been specifically rated, that rating.)*

3 [Notification

The UK Listing Authority [has been requested to provide/has provided - *include first alternative for an issue which is contemporaneous with the establishment or update of the Programme and the second alternative for subsequent issues] the [include names of competent authorities of host Member States*] with a certificate of approval attesting that the Prospectus has been drawn up in accordance with the Prospectus Directive.]

4 [INTERESTS OF NATURAL AND LEGAL PERSONS INVOLVED IN THE [ISSUE/OFFER]]

Need to include a description of any interest, including conflicting ones, that is material to the issue/offer, detailing the persons involved and the nature of the interest. May be satisfied by the inclusion of the following statement:

"Save as discussed in ["Subscription and Sale"], so far as the Issuer is aware, no person involved in the offer of the Bonds has an interest material to the offer."

5 Reasons for the offer, estimated net proceeds and total expenses

(i) [Reasons for the offer:	[●]

	(See *["Use of Proceeds"] wording in Prospectus – if reasons for offer different from making profit and/or hedging certain risks will need to include those reasons here.)]*
(ii) [Estimated net proceeds:	[●]
	(*If proceeds are intended for more than one use will need to split out and present in order of priority. If proceeds insufficient to fund all proposed uses state amount and sources of other funding*)]
(iii) [Estimated total expenses:	[●] (*Include breakdown of expenses.*)
	(*Only necessary to include disclosure of net proceeds and total expenses at (ii) and (iii) above where disclosure is included at (i) above*).][(1)]

6 [Fixed Rate Bonds only – YIELD

Indication of yield:	[●]
	The yield is calculated at the Issue Date on the basis of the Issue Price. It is not an indication of future yield.]

7 [Floating Rate Bonds Only - HISTORIC INTEREST RATES

Details of historic [LIBOR/EURIBOR/other] rates can be obtained from [Telerate].]

8 [Index-Linked or other variable-linked Bonds only – PERFORMANCE OF INDEX/FORMULA/OTHER VARIABLE AND OTHER INFORMATION CONCERNING THE UNDERLYING

Need to include details of where past and future performance and volatility of the index/formula/other variable can be obtained. Where the underlying is an index need to include the name of the index and a description if composed by the Issuer and if the index is not composed by the Issuer need to include details of where the information about the index can be obtained. Where the underlying is not an index need to include equivalent information.][(2)]

9 [*Dual currency Bonds only* – PERFORMANCE OF RATE[S] OF EXCHANGE

Need to include details of where past and future performance and volatility of the relevant rate[s] can be obtained.][(3)]

10 Operational information

ISIN Code:	[●]
Common Code:	[●]

Any clearing system(s) other than Euroclear Bank S.A./N.V. and Clearstream Banking Société Anonyme and the relevant identification number(s):	[Not Applicable/*give name(s) and member(s) [and address(es)*]
Delivery:	Delivery [against/free of] payment
Names and addresses of additional Paying Agent(s) (if any):	[●]

Notes:

(1) Required for derivative securities

(2) Required for derivative securities

(3) Required for derivative securities

CHAPTER 9
USE OF PROCEEDS

The net proceeds from each issue of Bonds under the Programme will be on-lent to SWS under the terms of further Issuer/SWS Loan Agreements to be applied by SWS for its general corporate purposes or used to repay or service the Issuer's Financial Indebtedness.

CHAPTER 10
MBIA AND ITS FINANCIAL GUARANTEES

MBIA UK INSURANCE LIMITED

General

MBIA UK Insurance Limited ("**MBIA**" or "**MBIA UK**") was incorporated with limited liability in England and Wales on 22 March 2002 pursuant to the Companies Act 1985 with registered number 04401508. MBIA UK became authorised by the Financial Services Authority ("**FSA**") to transact financial guarantee business in the United Kingdom on 18 May 2004 with FSA reference number 225326. Its registered office is located at 1 Great St Helen's, London, EC3A 6HX, United Kingdom (telephone: +44 (0)20 7920 6363).

MBIA UK is a direct wholly owned subsidiary of MBIA UK (Holdings) Limited ("**MBIA Holdings**") a limited liability company incorporated in England and Wales on 23 June 2003 with registered number 04808006, whose registered office is located at 1 Great St. Helen's, London EC3A 6HX. MBIA Holdings is a direct wholly owned subsidiary of MBIA Insurance Corporation ("**MBIA Corp.**"). MBIA Corp. is the principal operating subsidiary of MBIA Inc. ("**MBIA Inc.**"). MBIA Inc. is not obliged to pay the debts of, or claims against, MBIA Corp. or MBIA UK. MBIA UK has no subsidiaries.

Prior to the incorporation of MBIA UK as a limited liability company, the MBIA group operated in the United Kingdom both on a services and a branch basis through its French subsidiary, MBIA Assurance S.A. ("**MBIA Assurance**") by means of the EC third non-life insurance directive (No. 92/49/EEC). MBIA Assurance was registered as an overseas company in England and Wales under Chapter II of Part XXII of the Companies Act 1985 on 10 February 1997 under number FC020116 and a branch of MBIA Assurance was registered in the United Kingdom during 2000 under number BR003789.

Business

MBIA UK is engaged principally in the business of writing financial guarantee and related lines of insurance and reinsurance transactions. Financial guarantee insurance provides a guarantee of timely payments of scheduled principal and interest by the issuer of securities thereby enhancing the credit rating of those securities in return for the payment of a premium to the financial guarantor.

Regulation

MBIA UK's business in the United Kingdom is subject to regulation by the FSA.

MBIA UK is authorised by the FSA to carry out general insurance business of the following classes in the United Kingdom, namely credit insurance (Class 14), suretyship insurance (Class 15) and insurance against miscellaneous financial loss (Class 16) and any other kind of business to the extent it falls within the scope of or is in the course of carrying out, the above-mentioned activities for which MBIA UK is authorised to transact. MBIA UK carries out its activities in the

European Economic Area on a cross-border services basis in accordance with Section 37 of the Financial Services and Markets Act 2000 ("**FSMA**") and Part III of Schedule 3 to FSMA.

Under the FSA regulations, MBIA UK is subject to certain supervisory requirements including the maintenance of a minimum solvency margin and establishment and maintenance of loss and unearned premium reserves. In addition, other requirements of the FSA include an obligation to report on transactions entered into with connected persons, certain other transactions it enters into, the regulation of its investments and the on-going monitoring of its compliance with FSA rules.

Financial Strength Ratings

Fitch, Inc. ("**Fitch**"), Moody's Investor Service, Inc. ("**Moody's**") and Standard & Poor's, a division of The McGraw-Hill Companies, Inc. ("**S&P**") have rated the financial strength of MBIA UK at "AAA", "Aaa" and "AAA" respectively. The ratings of MBIA UK are based primarily on the ratings of and capital support provided by MBIA Corp. Any reduction in the ratings of MBIA Corp. would result in a downgrade of the ratings of MBIA UK and could have a material adverse effect on MBIA Corp. and MBIA UK.

Each rating of MBIA UK should be evaluated independently. The ratings reflect the respective rating agency's current assessment of the financial strength of MBIA UK and its ability to pay claims on its financial guarantees. Any further explanation as to the significance of the above ratings may be obtained only from the applicable rating agency.

The above ratings are not recommendations to buy, sell or hold the obligations, and such ratings may be subject to revision or withdrawal at any time by the rating agencies. Any downward revision or withdrawal of any of the above ratings may have an adverse effect on the market price of the obligations. MBIA UK does not guarantee the market price of the obligations nor does it guarantee that the ratings on the obligations will not be revised or withdrawn.

Summary of Financial Information and Recent Developments

During the year ending 31 December 2003, MBIA UK did not trade, did not incur any liabilities and consequently made neither a profit nor a loss. MBIA UK was dormant (within the meaning of section 249 AA Companies Act 1985) since its formation and at all times during and up to the year ending 31 December 2003. Consequently, it was not required to have its financial statements audited for the year ended 31 December 2003.

The company's issued share capital was increased to £68,000,000 on 10 May 2004; from that date until 31 December 2004 the company did not enter into any insurance transactions but generated a net profit from its investments. MBIA UK issued its first financial guarantee in July 2005.

Capitalisation and Indebtedness Table

As at 31 December 2005 the capitalisation and indebtedness of MBIA UK was as follows (*source: audited accounts of MBIA UK for financial year ended 31 December 2005*)

MBIA UK Insurance Limited – Capitalisation and Indebtedness Table[1]

	As at 31 December 2005	As at 31 December 2004	As at 31 December 2003
		(£)	
Assets			
Long-term investments	74,497,051	23,691,688	0
Current assets	26,499,439	47,377,479	1
Total assets	**100,996,490**	**71,069,167**	**1**
Indebtedness[2]			
Short term debt	6,862,794	1,912,710	0
Long term debt	1,399,790	0	0
Technical provisions	22,470,292	0	0
Total indebtedness	**30,732,876**	**1,912,790**	
Shareholders' Equity[3]			
Called up share capital	68,000,000	68,000,000	1
Reserves	2,263,614	1,156,457	0
Total Shareholders' Equity	**70,263,614**	**69,156,457**	**1**
Total Capitalisation and Indebtedness[4]	**100,996,490**	**71,069,167**	**1**

Notes:

(1) This Capitalisation and Indebtedness Table has been prepared in accordance with generally accepted accounting principles in the United Kingdom.

(2) On 31 December 2005, MBIA UK did not have any loan capital outstanding or created but unissued term loans or any other borrowings in the nature of borrowing, including bank overdrafts and liabilities under acceptances or acceptance credits, mortgages, charges, finance lease commitments, hire purchase obligations or guarantees, or contingent liabilities.

(3) MBIA UK was incorporated with an authorised share capital of £100,000,000 comprising 100,000,000 ordinary shares of £1 each. As at 31 December 2003, 1 ordinary share of £1 had been allotted but not paid. On 10 May 2004, MBIA UK issued fully paid up share capital of a further 67,999,999 ordinary shares of £1 each. MBIA UK did not write premia in the year ended 31 December 2004, but generated a gross profit from investment and interest income and incurred a resulting tax expense and short-term liability.

(4) There has been no material change in the authorised and issued share capital, capitalisation, indebtedness, contingent liabilities or guarantees of MBIA UK since 31 December 2005.

Directors and Officers

The directors of MBIA UK and their principal activities as at the date of this disclosure statement are set out below:

Name:	Function:	Principal Activities:
Neil G. Budnick	Executive	Chief Executive Officer: MBIA UK. Director: Capital Markets Assurance Corporation, MBIA Insurance Corporation, MBIA International Marketing Services, Pty. Limited, MBIA UK (Holdings) Limited, Channel Re. Director: Association of Financial Guaranty Insurers (AFGI).
Kenneth G. Cox	Non-Executive	Director: MBIA UK. Non-executive Director: Penstock Asset Management Limited (Jersey) and ING RPFI Management Limited (Geneva). Executive Director: Assettrust Housing Limited, Assettrust Housing Investments Limited, Assettrust Housing Projects Limited, AHL Langley Holdings Limited, AHL Langley Investment Limited, AHL Langley Trading Limited, AHL Point Pleasant Trading Limited, AHL Woolwich Arsenal Trading Limited.
C. Edward Chaplin	Executive	Chief Financial Officer: MBIA UK. Director: Capital Markets Assurance Corporation, MBIA Insurance Corporation, MBIA UK (Holdings) Limited.
Gary C. Dunton	Executive	Managing Director: MBIA UK. Director: Capital Markets Assurance Corporation, MBIA Assurance S.A., MBIA Inc, MBIA Insurance Corporation, Euro Asset Acquisition Ltd, MBIA UK (Holdings) Limited.
Philip C. Sullivan	Executive	Chief Risk Officer and Managing Director: MBIA UK. Director: MBIA Assurance S.A., MBIA UK (Holdings) Limited.
Andrew F. Sykes	Non-Executive	Director: MBIA UK. Chairman: Insight Foundation Property Trust Limited and Absolute Return Trust Limited. Director: JPMorgan Fleming Asian Investment Trust Limited, Schroder Exempt Property Unit Trust, Schroder Executor & Trustee Co, Smith & Williamson

Name:	Function:	Principal Activities:
		Holdings Limited and Gulf International Bank Limited.
		Member of the Advisory Committee of SVG Diamond Holdings Limited.
Christopher E. Weeks	Executive	President and Managing Director: MBIA UK.
		Director: MBIA UK (Holdings) Limited.
Ram D. Wertheim	Executive	Joint Company Secretary and Managing Director: MBIA UK.
		Director: Capital Markets Assurance Corporation, MBIA Insurance Corporation, MBIA Assurance SA, MBIA UK (Holdings) Limited.
Deborah M. Zurkow	Executive	Managing Director: MBIA UK.
		President and Directeur Général MBIA Assurance S.A..
		Director: MBIA UK (Holdings) Limited.
Gerald H. C. Wakefield	Non-Executive	Director: MBIA UK.

The principal executive officers of MBIA UK are set out below:

Neil G. Budnick	Chief Executive Officer
Christopher E. Weeks	President
C. Edward Chaplin	Chief Financial Officer
Phillip C. Sullivan	Chief Risk Officer
Ram D. Wertheim	Joint Company Secretary
Sabrina B. Biscardi	Joint Company Secretary, Legal Compliance Officer, General Counsel
Juliet S. Telford	Financial Compliance Officer, Controller
Kathleen M. Reagan	Internal Auditor

The principal executive offices of MBIA UK are located at 1 Great St Helen's, London, EC3A 6HX, United Kingdom and its telephone number at this address is +44 (0)20 7920 6363. The business address of Messrs. Dunton, Chaplin and Wertheim is 113 King Street, Armonk, New York 10504, United States of America.

As at the date of this Prospectus, the above-mentioned board members of MBIA UK do not have potential conflicts of interest, material to the Bonds, between any duties to MBIA UK, and their private interests or other duties.

Risk Diversification

MBIA Corp. and MBIA UK seek to maintain a diversified insured portfolio designed to spread risk based on a variety of criteria, including revenue source, issue size, type of bond and geographic area. As at 31 December 2005, MBIA Corp. had 27,081 policies outstanding. These policies are diversified among 10,717 "credits", which MBIA Corp. and its subsidiaries define as any group of issues supported by the same revenue source.

Reinsurance

In the ordinary course of its business, MBIA UK uses reinsurance as a risk management device to reinsure financial guarantees with third party reinsurers primarily to transfer risk and to increase underwriting capacity. MBIA UK uses both treaty and facultative reinsurance to cede risk. Under its treaties with various reinsurers, MBIA UK has the ability to automatically cede specified percentages of insured risks as provided for in each treaty. To the extent MBIA UK needs reinsurance capacity that is not available under its treaties, it cedes risk to reinsurers on a facultative basis where reinsurers have considered the commitment and decided to provide the reinsurance outside the terms of the treaty.

As a primary guarantor, MBIA UK is required to honour its obligations to the holders of its financial guarantees whether or not its reinsurers perform their obligations to MBIA UK.

Auditors

MBIA UK's auditors are PricewaterhouseCoopers LLP of 32 London Bridge Street, London SE1 9SY. PricewaterhouseCoopers LLP is a partnership of chartered accountants and registered auditors and a member of the Institute of Chartered Accountants in England and Wales.

MBIA UK, having been dormant within the meaning of section 249AA Companies Act 1985 since its formation and at all times during the year ended 31 December 2003, and otherwise satisfying the relevant requirements of Part VII of the Companies Act 1985, was exempt from the provisions of that Part relating to the audit of accounts for the year ended 31 December 2003.

Copies of MBIA UK's audited accounts are available from The Company Secretary, MBIA UK Insurance Limited, 1 Great St. Helen's, London EC3A 6HX.

Relationship between MBIA UK and MBIA Corp.

MBIA UK and MBIA Corp. have entered into an excess of loss reinsurance agreement dated 14 May 2004 (the "**Excess of Loss Reinsurance Agreement**"). MBIA Corp., MBIA Holdings and MBIA UK have entered into a Net Worth Maintenance agreement dated 14 May 2004 (as amended and restated on 12 October 2004) (the "**Net Worth Maintenance Agreement**"). The purpose of the Excess of Loss Reinsurance Agreement and the Net Worth Maintenance Agreement is to provide MBIA UK with additional capital and reinsurance support in the event of excess losses not covered by its available capital and by third party reinsurance.

Under the Excess of Loss Reinsurance Agreement, MBIA Corp. agrees to reinsure on an excess of loss basis all financial guarantees issued by MBIA UK. Under the Excess of Loss Reinsurance

Agreement MBIA Corp. will reimburse MBIA UK, on an excess of loss basis, for losses exceeding $100,000,000 in aggregate incurred in each calendar year for its net retained insurance liability (being MBIA UK's gross liability on each guarantee reinsured by MBIA Corp. after deducting all cessions to facultative and/or other reinsurers, the "**Net Retained Liability**") under all financial guarantees issued by MBIA UK. MBIA Corp.'s maximum liability under the Excess of Loss Reinsurance Agreement shall not exceed 20% of MBIA UK's Net Retained Liability with respect to the aggregate insured principal sum outstanding as of 11:59pm, Greenwich Mean Time, on 31 December of the prior year plus the insured principal sum outstanding under MBIA UK's two largest financial guarantees in effect as of 11:59 pm, Greenwich Mean Time on 31 December of the prior year.

The reinsurance provided under the Excess of Loss Reinsurance Agreement does not alter or limit the obligations of MBIA UK under any financial guarantee.

Pursuant to the Net Worth Maintenance Agreement, MBIA Corp. and MBIA Holdings agree to maintain capital in MBIA UK in an amount that is at least equal to $100,000,000 or such greater amount as shall be required now or in the future to comply with statutory and regulatory requirements in the United Kingdom. Any support provided by MBIA Corp. to MBIA UK is subject to compliance with New York insurance law. MBIA Corp. may not contribute more than 35% of its policyholders' surplus on an accumulated basis and must comply with §1505 of the New York State Insurance Law, which requires prior notification to and approval by the New York State Insurance Department for any additional capital contributions. MBIA Corp. may, however, make single contributions to MBIA UK that do not exceed $300 million each without taking any additional actions under §1505 of the New York Insurance Law. As at 31 December 2005, the policyholders' surplus for MBIA Corp. was approximately $3.800 billion.

Bondholders should note that the Excess of Loss Reinsurance Agreement and the Net Worth Maintenance Agreement (the "**MBIA UK Agreements**") are entered into for the benefit of MBIA UK and are not, and should not be regarded as, guarantees by MBIA Corp. of the payment of any indebtedness, liability or obligations of the issuer, the bonds or any MBIA financial guarantee. Notwithstanding the capital support provided to MBIA UK described in this section, the MBIA UK Agreements do not confer any rights on third parties. Beneficiaries of any MBIA financial guarantee will have direct recourse against MBIA UK only, and neither MBIA Corp. nor any other affiliate thereof will be directly liable to the beneficiaries of any MBIA UK financial guarantee.

The information in this disclosure statement concerning MBIA Corp. and its affiliates is provided for background purposes only in view of the importance to MBIA UK of the MBIA UK Agreements. It does not imply that the MBIA UK Agreements are guarantees for the benefit of the beneficiaries of any MBIA UK financial guarantee. Payments of principal and interest on the obligations will be guaranteed by MBIA UK pursuant to the terms of the financial guarantees provided by MBIA UK and will not be additionally guaranteed by either MBIA Corp. or any other affiliate.

The MBIA UK Agreements are intracompany agreements and do not confer rights on third parties; however, these arrangements, together with the ownership of MBIA UK by MBIA Corp. and the underwriting support supplied to MBIA UK by MBIA Corp., may make information

about MBIA Corp. of interest to the beneficiaries of financial guarantees issued by MBIA UK. Additionally, the MBIA UK Agreements were relevant to the rating agencies in justification of the triple-A ratings granted to MBIA UK. Any material modifications to the Net Worth Maintenance Agreement are subject to confirmation from each of the rating agencies that such modifications will not result in the reduction or withdrawal of the claims-paying ratings then assigned to MBIA UK.

Pursuant to procedures initially developed by MBIA Corp., MBIA UK is selective in the risks it chooses to guarantee. Logistic and underwriting support is supplied to MBIA UK from MBIA Corp. The logistic review of a credit and the proposed structure is undertaken by analysts on a deal team. Both the credit and the structure are then presented to a separate underwriting committee composed of persons not directly involved in the initial analysis. Only following approval of both the credit and the structure may a financial guarantee be issued by MBIA UK.

MBIA Corp. and MBIA UK maintain zero-loss underwriting standards; they underwrite their respective financial guarantees such that at the time a financial guarantee is issued no losses are expected throughout the term of the guarantee based on a worst-case scenario.

Material Contracts

Save as disclosed in this Prospectus (see "*Relationship between MBIA UK and MBIA Corp.*"), MBIA UK has not entered into contracts outside the ordinary course of business that could result in MBIA UK being under an obligation or entitlement that is material to MBIA UK's ability to meet its obligations to the beneficiary of its financial guarantee.

MBIA INSURANCE CORPORATION

General

MBIA Corp. is a leading global provider of financial guarantee insurance incorporated in the State of New York whose registered office is at 113 King Street, Armonk, NY 10504, United States of America. MBIA Corp. is a wholly owned subsidiary of MBIA Inc., which is engaged in providing financial guarantee insurance and investment management and financial services to public finance clients and financial institutions on a global basis. MBIA Corp. provides financial guarantee insurance policies for municipal bonds, asset-backed and mortgage-backed securities, investor-owned utility bonds, and collateralised obligations of sovereigns, corporations and financial institutions, both in the new issue and secondary markets. MBIA Corp. also insures privately issued bonds used for the financing of public purpose projects which are primarily located overseas and include toll roads, bridges, airports, public transportation facilities and other types of infrastructure projects that serve a substantial public purpose. While in the United States projects of this nature are financed through the issuance of tax-exempt bonds by special purpose, government sponsored tax-exempt entities, the general absence of tax-advantaged financing, among other reasons, has led to the transfer of the operation of many such public purpose projects to the private sector. Generally, the private entities operate under a concession agreement with the sponsoring government agency, which maintains a level of regulatory oversight and control over the project.

MBIA Corp. is the successor to the business of the Municipal Bond Insurance Association (the "**Association**") which began writing financial guarantees for municipal bonds in 1974. MBIA Corp. is the parent of MBIA Corp. of Illinois ("**MBIA Illinois**") and Capital Markets Assurance Corporation ("**CapMAC**"), both financial guarantee companies. In 1990, MBIA Corp. formed a French insurance company, MBIA Assurance, to write financial guarantee insurance in the countries of the European community. MBIA Assurance, which is a 99.99% subsidiary of MBIA Corp., writes financial guarantees insuring sovereign risk, public infrastructure financings, asset-backed transactions and certain collateralised obligations of corporations and financial institutions. MBIA Assurance has used the provisions of the EC third non-life insurance directive (No. 92/49/EEC) to operate in the United Kingdom both on a services and a branch basis. In light of the amount of business generated from the United Kingdom, MBIA UK was created in 2002 and received regulatory authorization in 2004. Generally, throughout the text, references below to MBIA Corp. include the activities of its subsidiaries, MBIA Illinois, MBIA Assurance, MBIA UK and CapMAC.

Financial guarantee insurance provides an unconditional and irrevocable guarantee of the payment of the principal and interest or other amounts owing, on insured obligations when due. MBIA Corp. primarily insures obligations which are sold in the new issue and secondary markets, or which are held in unit investment trusts ("**UIT**") and by mutual funds. It also provides surety bonds for debt service reserve funds. The principal economic value of financial guarantee insurance to the entity offering the obligations is the savings in interest costs resulting from the difference in the market yield between an insured obligation and the same obligation on an uninsured basis. In addition, for complex financings and for obligations of issuers that are not well-known by investors, insured obligations receive greater market acceptance than uninsured obligations. The municipal obligations that MBIA Corp. insures include tax-exempt and taxable indebtedness of states, counties, cities, utility districts and other political subdivisions, as well as airports, higher education and health care facilities and similar authorities. The asset-backed or structured finance obligations insured by MBIA Corp. typically consist of securities that are payable from or which are tied to the performance of a specified pool of assets that have a defined cash flow. These include residential and commercial mortgages, a variety of consumer loans, corporate loans and bonds and equipment and real property leases.

Financial Strength Ratings of MBIA Corp.

Fitch, Moody's and S&P have rated the financial strength of MBIA Corp. at "AAA", "Aaa" and "AAA" respectively.

Each rating of MBIA Corp. should be evaluated independently. The ratings reflect the respective rating agency's current assessment of the creditworthiness of MBIA Corp. and its ability to pay claims on its financial guarantees. Any further explanation as to the significance of the above ratings may be obtained only from the applicable rating agency.

Capitalisation and Indebtedness Table

The following table sets forth the capitalisation and indebtedness of MBIA Corp. as at 31 December 2005, 31 December 2004 and 31 December 2003 (*source: extracted from the audited accounts of MBIA Corp. for financial years ended 31 December 2005, 2004 and 2003*):

	31 December 2005	31 December 2004	31 December 2003
	(US$ in thousands)		
Long-term Debt	Nil	Nil	Nil
Investors' Equity:			
Common stock, par value $150 per share; authorised,			
issued and outstanding – 100,000 shares	15,000	15,000	15,000
Additional paid-in capital	1,672,310	1,654,201	1,636,422
Capital Contribution	Nil	Nil	Nil
Retained earnings	5,202,304	4,526,601	4,405,658
Accumulated other comprehensive income.	190,286	381,547	437,993
Total Investors' Equity	US$7,079,900	US$6,577,349	US$6,495,073
Total Capitalisation and Indebtedness (2)	US$7,079,900	US$6,577,349	US$6,495,073

(1) Represents the additional contribution from MBIA Inc. above the par value of the common stock.

(2) There has been no material change in the authorized and issued share capital, in the capitalisation and indebtedness, contingent liabilities or guarantees of MBIA Corp. since 31 December 2005.

Risk Diversification

At 31 December 2005, the net par amount outstanding on MBIA Corp.'s insured obligations (including insured obligations of MBIA Illinois, MBIA Assurance and CapMAC, but excluding the guarantee of US$15.6 billion of investment management transactions for MBIA Investment Management Corp. and MBIA Global Funding Limited) was US$585.0 billion. Net insurance in force was US$889.0 billion.

Because generally MBIA Corp. guarantees to the holder of the underlying obligation the timely payment of amounts due on such obligation in accordance with its original payment schedule, in the case of a default on an insured obligation, payments under the financial guarantee cannot be accelerated unless MBIA Corp. consents to the acceleration. Otherwise, MBIA Corp. is required to pay principal, interest or other amounts only as originally scheduled payments come due.

MBIA Corp. underwrites financial guarantee insurance on the assumption that the insurance will remain in force until maturity of the insured obligations. MBIA Corp. estimates that the average life (as opposed to the stated maturity) of its insurance policies and financial guarantees in force at 31 December 2005 was 10.4 years. The average life was determined by applying a weighted average calculation, using the remaining years to maturity of each insured obligation, and weighting them on the basis of the remaining debt service insured. No assumptions were made

for any future refundings of insured issues. Average annual debt service on the portfolio at 31 December 2005 was US$ 69.5 billion.

Reinsurance

State insurance laws and regulations, as well as the rating agencies, impose minimum capital requirements on financial guarantee companies, limiting the aggregate amount of insurance which may be written and the maximum size of any single risk exposure which may be assumed. MBIA Corp. increases its capacity to write new business by using treaty and facultative reinsurance to reduce its gross liabilities on an aggregate and single risk basis.

As a primary insurer, MBIA Corp. is required to honour its obligations to its policyholders whether or not its reinsurers perform their obligations to MBIA Corp. The financial position of all reinsurers is monitored by MBIA Corp. on a regular basis.

Regulation

MBIA Corp. is licensed to do insurance business in, and is subject to insurance regulation and supervision by, the State of New York (its state of incorporation), the 49 other US states, the District of Columbia, the Territory of Guam, the Commonwealth of the Northern Mariana Islands, the Virgin Islands of the United States, the Commonwealth of Puerto Rico, the Kingdom of Spain, the Republic of France, the United Kingdom and the Republic of Singapore. The extent of state insurance regulation and supervision varies by jurisdiction, but New York, Illinois and most other jurisdictions have laws and regulations prescribing minimum standards of solvency, including minimum capital requirements and business conduct which must be maintained by insurance companies. The laws and regulations of these states also limit both the aggregate and individual risks that MBIA Corp. may insure on a net basis based on the type of risk being insured. These laws prescribe permitted classes and concentrations of investments. In addition, some state laws and regulations require the approval or filing of policy forms and rates. MBIA Corp. is required to file detailed annual financial statements with the New York Insurance Department and similar supervisory agencies in each of the other jurisdictions in which it is licensed. The operations and accounts of MBIA Corp. are subject to examination by these regulatory agencies at regular intervals. MBIA Inc. is subject to the direct and indirect effects of governmental regulation, including changes in tax laws affecting the municipal and asset-backed debt markets. No assurance can be given that future legislative or regulatory changes might not adversely affect the results of operations and financial conditions of MBIA Inc.

MBIA Corp. is licensed to provide financial guarantee insurance under Article 69 of the New York Insurance Law. Article 69 defines financial guarantee insurance to include any guarantee under which loss is payable upon proof of occurrence of financial loss to an insured as a result of certain events. These events include the failure of any obligor on or any issuer of any debt instrument or other monetary obligation to pay principal, interest, premium, dividend or purchase price of or on such instrument or obligation, when due. Under Article 69, MBIA Corp. is licensed to transact financial guarantee insurance. In addition, MBIA Corp. is empowered to assume or reinsure the kinds of insurance that it is licensed to write directly.

As a financial guarantee insurer, MBIA Corp. is required by the laws of New York, California, Connecticut, Florida, Illinois, Iowa, New Jersey and Wisconsin to maintain contingency reserves on its municipal bonds, asset-backed securities and other financial guarantee liabilities. Under New Jersey, Illinois and Wisconsin regulations, contributions by such an insurer to its contingency reserves are required to equal 50% of earned premiums on its municipal bond business. Under New York law, such an insurer is required to contribute to contingency reserves 50% of premiums as they are earned on policies and financial guarantees written prior to 1 July 1989 (net of reinsurance) and, with respect to policies and financial guarantees written on and after 1 July 1989, must make contributions over a period of 15 or 20 years (based on issue type), or until the contingency reserve for such insured issues equals the greater of 50% of premiums written for the relevant category of insurance or a percentage of the principal guaranteed, varying from 0.55% to 2.5%, depending upon the type of obligation guaranteed (net of reinsurance, refunding, refinancing and certain insured securities). California, Connecticut, Iowa and Florida law impose a generally similar requirement. In each of these states, MBIA Corp. may apply for release of portions of the contingency reserves in certain circumstances.

The laws of New York regulate the payment of dividends by MBIA Corp. and provide that a New York domestic stock property/casualty insurance company (such as MBIA Corp.) may not declare or distribute dividends except out of statutory earned surplus. New York law provides that the sum of (i) the amount of dividends declared or distributed during the preceding 12-month period and (ii) the dividend to be declared may not exceed the lesser of (a) 10% of policyholders' surplus, as shown by the most recent statutory financial statement on file with the New York Insurance Department, and (b) 100% of adjusted net investment income for such 12-month period (the net investment income for such 12-month period plus the excess, if any, of net investment income over dividends declared or distributed during the two-year period preceding such 12-month period), unless the New York Superintendent of Insurance approves a greater dividend distribution based upon a finding that the insurer will retain sufficient surplus to support its obligations and writings. The foregoing dividend limitations are determined in accordance with Statutory Accounting Practices ("**SAP**"), which generally produce statutory earnings in amounts less than earnings computed in accordance with Generally Accepted Accounting Principles ("**GAAP**"). Similarly, policyholders' surplus, computed on a SAP basis, will normally be less than net worth computed on a GAAP basis.

MBIA Corp., MBIA Illinois and CapMAC are exempt from assessments by the insurance guarantee funds in the majority of the states in which they do business. Guarantee fund laws in most states require insurers transacting business in the state to participate in guarantee associations, which pay claims of policyholders and third-party claimants against impaired or insolvent insurance companies doing business in the state. In most cases, insurers licensed to write only municipal bond insurance, financial guarantee insurance and other forms of surety insurance are exempt from assessment by these funds and their policyholders are prohibited from making claims on these funds.

Management

At 4 May 2006, the principal executive officers and their present ages and positions within MBIA Corp. are set forth below:

Name	Age	Position
Gary C. Dunton	51	Chairman and Chief Executive Officer
Neil G. Budnick	52	President
Ram D. Wertheim	51	Managing Director, General Counsel and Secretary
C. Edward Chaplin	50	Managing Director and Chief Financial Officer
Ruth M. Whaley	50	Managing Director and Chief Risk Officer
Mitch I. Sonkin	53	Managing Director and Head of Insured Portfolio Management
William C. Fallon	46	Managing Director and Head of Corporate Strategy and Communications
Christopher E. Weeks	45	Managing Director and Head of International
Willard I. Hill, Jr.	50	Managing Director and Chief Compliance Officer
Douglas C. Hamilton	57	Managing Director and Controller
Thomas G. McLoughlin	45	Managing Director and Head of Public Finance
Andrea E. Randolph	53	Managing Director and Chief Technology Officer
Kevin D. Silva	52	Managing Director and Chief Administrative Officer
Richard Thevenet	50	Managing Director and Treasurer
Clifford D. Corso	44	Managing Director and Chief Investment Officer
Mark S. Zucker	57	Managing Director and Head of Structured Finance

Recent Developments[(1)]

For the quarter ended 30 June 2006, MBIA Corp. had net income of US$208.1 million as compared to US$197.6 million for the quarter ended 30 June 2005. At 30 June 2006, MBIA Corp.'s investor's equity was US$7.1 billion.

MBIA Corp. guaranteed US$39.8 billion of net par value through the second quarter of 2006, a decrease of 27.8% over the US$55.1 billion of net par insured in the same 2005 period. During the first two quarters of 2006, MBIA Corp. insured US$19.4 billion of net par value of domestic municipal bonds, a 41.0% decrease from US$32.9 billion insured in the same 2005 period. In the domestic structured finance market, which includes mortgage-backed and asset-backed transactions, MBIA Corp. insured US$12.0 billion of net par value in the first two quarters of 2006, an increase of 4.3% from the US$11.5 billion insured in the first two quarters of 2005. In addition, MBIA Corp. insured US$8.4 billion of net securities internationally during the first two quarters of 2006 compared with US$10.7 billion insured in the first two quarters of 2005.

Gross premiums written in the second quarter of 2006 increased to US$258.4 million from US$256.9 million written in the second quarter of 2005. Net premiums earned during the second quarter of 2006 were US$221.5 million, down from US$218.4 million earned in the second quarter of 2005. Net investment income, excluding net realized capital gains, increased from

US$120.2 million in the second quarter of 2005 to US$138.4 million in the second quarter of 2006. Revenues of MBIA Corp. for the quarter ended 30 June 2006 increased to US$378.5 million compared with US$341.7 million for the quarter ended 30 June 2005. Total expenses for the quarter ended 30 June 2006 were US$88.0 million compared to US$70.4 million for the quarter ended 30 June 2005.

Computed on a statutory basis, as of 30 June 2006, MBIA Corp.'s unearned premium reserve was US$3.5 billion, and its capital base, consisting of capital and surplus and contingency reserve, was US$6.7 billion. Total claims-paying resources at 30 June 2006 and 30 June 2005 were US$13.5 billion and US$13.0 billion, respectively.

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(1) The source of the financial information appearing in the section entitled "Recent Developments" is MBIA Corp.'s books and records.

MBIA FINANCIAL GUARANTEE

Financial Guarantee Number:	[•]
Guaranteed Obligations:	The payment obligations of the Issuer in respect of each amount of Principal and Interest owing by the Issuer and outstanding under the Bonds, as further defined below.
Guarantor:	MBIA UK Insurance Limited, a private limited company incorporated under the laws of England and Wales with registered number 04401508 whose registered office is at 1 Great St. Helen's, 2nd Floor, London EC3A 6HX ("**MBIA**").
Beneficiary:	The Bond Trustee
Date of Issue:	[•]

1. DEFINITIONS, INTERPRETATION AND CONSTRUCTION

1.1 Definitions

For the purposes of this Financial Guarantee, the following terms will have the meanings given to them below:

"**Accelerated Payment**" means, following an Acceleration, any payment in full or in part by MBIA of the Guaranteed Obligations in advance of the relevant Payment Date.

"**Acceleration**" means, in relation to the Bonds, when the Bonds are immediately due and payable pursuant to Condition 11(a) or 11(d), and "**Accelerated**" will be construed accordingly.

"**Affiliate**" means any person who directly or indirectly through one or more intermediaries controls, or is controlled by, or is under common control with, the first person, where "**control**" means the possession, directly or indirectly, of the power to direct or cause the direction of the management or policies of a person, whether through the ownership of voting stock, by contract or otherwise.

"**Agency Agreement**" has the meaning given to it in the Conditions.

"**Bonds**" means the Class A Wrapped Bonds.

"**Bond Trustee**" means Deutsche Trustee Company Limited or any additional or successor trustee appointed pursuant to the Bond Trust Deed.

"**Bond Trust Deed**" has the meaning given to it in the Conditions.

"**Business Day**" means any day other than (i) a Saturday or a Sunday, (ii) a legal holiday in London, or (iii) a day on which banking institutions in London are authorised or obliged by law or executive order to be closed.

"**Class A Wrapped Bonds**" means the Issuer's [Sub-Class [•] £//$ [•][•]%/Floating Rate/[•]% Index Linked] Guaranteed Class A Wrapped Bonds due [•].

"**Conditions**" means the terms and conditions of the Bonds, as set out in the Bond Trust Deed.

"**Due for Payment**" means due for payment on a Payment Date. For the avoidance of doubt "**Due for Payment**" does not include any date which may arise earlier than a Payment Date by reason of prepayment, Acceleration, mandatory or optional redemption or otherwise unless MBIA has given its prior written consent to such earlier date.

"**Financial Guarantee Fee**" has the meaning given to it in the Guarantee and Reimbursement Agreement.

"**Guaranteed Amounts**" means, with respect to any Payment Date, the sum of Interest and Principal (if any) due on the Guaranteed Obligations on such Payment Date and, for the avoidance of doubt, includes Recovered Amounts. "**Guaranteed Amounts**" does not include and no guarantee is given by MBIA under this Financial Guarantee in respect of any deduction or withholding which the Issuer may or would have been required to make for or on account of Taxes in respect of the Guaranteed Obligations, any gross-up or make whole payment payable by the Issuer in respect of any such deduction or withholding or any other amount payable by the Issuer in respect of Taxes due in connection with the payment of such amount of Principal and/or Interest.

"**Guarantee and Reimbursement Agreement**" means the agreement between inter alia, the Issuer and MBIA pursuant to which, *inter alia*, MBIA has agreed to issue the Financial Guarantee and the Issuer has agreed, *inter alia*, to indemnify MBIA for, and to MBIA being subrogated to the rights of the Holders and the Bond Trustee in respect of, any payments made by MBIA under the Financial Guarantee.

"**Guaranteed Obligations**" means the payment obligations of the Issuer in respect of each amount of Principal and Interest owing by the Issuer and outstanding and Due for Payment under the Class A Wrapped Bonds.

"**Holder**" shall mean if and to the extent the Guaranteed Obligations are represented by definitive bonds held outside of the Euroclear system operated by Euroclear S.A./N.A. ("**Euroclear**") and Clearstream Banking, *société anonyme* ("**Clearstream, Luxembourg**" and together with Euroclear and any additional or substitute clearing system from time to time nominated by the Issuer and/or Bond Trustee and approved by MBIA, the "**Clearing Systems**"), the bearers thereof and if and to the extent the Guaranteed Obligations are represented by a temporary or permanent global bond or definitive bonds held in a Clearing System, the persons for the time being shown in the records of the relevant Clearing System (other the Euroclear if Euroclear shall be an accountholder of Clearstream, Luxembourg and other than Clearstream, Luxembourg if Clearstream, Luxembourg shall be an accountholder of Euroclear) as being holders of Guaranteed Obligations (each an "**accountholder**") in which regard any certificate or other document issued by the relevant Clearing System as to the principal amount of the Guaranteed

Obligations standing to the account of any accountholder shall be conclusive and binding for all purposes hereof.

"**Interest**" means any amount in respect of regularly scheduled interest (as adjusted for indexation in accordance with the Conditions, if applicable) owing by the Issuer under the Bonds as set out in Condition 6, excluding any amount relating to prepayment, acceleration, early redemption, broken funding indemnities, penalties, default interest, premium, deferral, Taxes or similar types of payments or any amounts by which the Margin on the coupon on such Class A Wrapped Bonds exceeds the initial Margin on the coupon as at the date on which such Class A Wrapped Bonds were issued.

"**Issuer**" means Southern Water Services (Finance) Limited, a company incorporated as an exempted company with limited liability in the Cayman Islands with registered number 112331.

"**Insolvency Law**" means in respect of any Person, any applicable law in respect of the bankruptcy, insolvency, receivership, winding up, dissolution, reorganisation, administration or other arrangement for the benefit of the creditors, generally of such persons.

"**Margin**" has the meaning given to it in the Conditions.

"**Master Definitions Agreement**" means the master definitions agreement dates 23 July 2003 between, among others, MBIA, the Bond Trustee and the Issuer, as amended with the consent of MBIA from time to time.

"**MBIA Additional Amounts**" has the meaning given to that term in Clause 6 (*Withholding and Deductions*).

"**Nonpayment**" means, on any Payment Date, the failure by the Issuer to pay all or any part of the Guaranteed Amounts which are Due for Payment.

"**Notice of Demand**" means the notice of demand substantially in the form set out in the Schedule to this Financial Guarantee.

"**Order**" means a final, non-appealable order from a court of competent jurisdiction.

"**Participating Member State**" means a member state of the European Community that adopts or has adopted the euro as its lawful currency under the legislation of the European Union for European Monetary Union.

"**Paying Agent**" has the meaning given to it in the Conditions.

"**Payment Date**" means:

(a) in respect of Interest, an Interest Payment Date (as defined in Condition 6(i);

(b) in respect of Principal, the scheduled date(s) for repayment specified in Conditions 8(a) and 8(g);

(c) any earlier date for the payment of Interest or repayment of Principal to which MBIA shall have consented at its sole discretion; and

(d) with respect to Recovered Amounts, the date on which such Recovered Amounts are due and payable by the Bond Trustee or as the case my be, the Holder, pursuant to an Order.

"**Person**" means any individual, corporation, partnership, joint venture, association, joint stock company, trust (including any beneficiary thereof), unincorporated organisation or government or any agency or political sub-division thereof.

"**Preference**" means a preference pursuant to the relevant Insolvency Law.

"**Principal**" means each amount of regularly scheduled principal outstanding under the relevant Class A Wrapped Bonds (as adjusted for indexation in accordance with the Conditions, if applicable), as reduced by each amount of principal repaid or prepaid by the Issuer pursuant to the Conditions, excluding any amount relating to prepayment, acceleration, early redemption, broken-funding indemnities, mandatory costs, increased costs, penalties, premium, default interest, "spens" or similar types of payments.

"**Principal Financial Centre**" means the principal financial centre for the Relevant Currency, or if the Relevant Currency is euro, the principal financial centre of any Participating Member State.

"**Principal Paying Agent**" has the meaning given to it in the Conditions.

"**Receipt**" means (i) actual delivery by registered mail or personally to MBIA at the address set out in the Notice of Demand (or such other address as MBIA has notified in writing to the Bond Trustee by at least seven (7) Business Days' notice) prior to 12.00 noon, London time, on a Business Day or (ii) if such actual delivery takes place either on a day that is not a Business Day or after 12.00 noon, London time, "**Receipt**" will be deemed to have occurred on the next succeeding Business Day. If any notice or certificate (including any Notice of Demand) given hereunder to MBIA is not in proper form or is not properly completed, executed or delivered, MBIA shall not be deemed to have "**Received**" it.

"**Recovered Amounts**" means any Guaranteed Amount that was Due for Payment and was paid by or on behalf of the Issuer to the Bond Trustee or a Holder to the extent it has been deemed a Preference by an Order and recovered from the Bond Trustee or, as the case may be, the Holder by the receiver, conservator, debtor-in-possession or trustee in bankruptcy or other insolvency or similar official for the Issuer named or identified in the Order, and has not been paid or recovered from any other source.

"**Relevant Currency**" means the relevant currency of the Bonds.

"**Taxes**" includes all present and future income, turnover and other taxes, levies, imposts, deductions, charges and withholdings whatsoever imposed, charged or levied by any jurisdiction or any governmental or taxing authority (including without limitation, any insurance, stamp, registration, issue or documentary taxes or duties) together with interest thereon and penalties with respect thereto (if any) and any payments of principal, interest, charges, fees or other amounts made on or in respect thereof and "**Tax**" and "**Taxation**" will be construed accordingly.

"**Termination Date**" has the meaning set out in Clause 14.1.

"**Transaction Documents**" has the meaning given to it in the Master Definitions Agreement.

1.2 **Interpretation**

In this Financial Guarantee, a reference to:

1.2.1 a statutory provision includes a reference to the statutory provision as modified or re-enacted or both from time to time whether before or after the date of this Financial Guarantee and any subordinate legislation made or other thing done under the statutory provision whether before or after the date of this Financial Guarantee;

1.2.2 a document is a reference to that document as modified, supplemented or replaced from time to time;

1.2.3 a Person includes a reference to a government, state, state agency, corporation, body corporate, association or partnership;

1.2.4 a Person includes a reference to that Person's legal personal representatives, successors and permitted assigns;

1.2.5 the singular includes the plural and *vice versa* (unless the context otherwise requires);

1.2.6 a time of day is a reference to the time in London, unless a contrary indication appears; and

1.2.7 a clause or schedule, unless the context otherwise requires, is a reference to a clause of or schedule to this Financial Guarantee.

1.3 **Headings**

Headings and sub-headings are for ease of reference only and will not affect the construction of this Financial Guarantee.

2. **GUARANTEE**

2.1 MBIA unconditionally and irrevocably guarantees to the Bond Trustee for the benefit of the Holders of the Guaranteed Obligations:

2.1.1 an amount equal to the Guaranteed Amounts which have become Due for Payment but are unpaid by reason of Nonpayment; and

2.1.2 an amount equal to the Guaranteed Amounts which are Recovered Amounts.

2.2 This Financial Guarantee does not guarantee any prepayment or other acceleration payment which at any time may become due in respect of any Guaranteed Obligation, other than at the sole option of MBIA as specified in Clause 7 (*Acceleration*), nor against any risk other than Nonpayment, including failure of the Bond Trustee or any Paying Agent to make any payment due to Holders of Guaranteed Amounts nor any amount in respect of any deduction or withholding which the Issuer would have been required to make for or on account of Taxes in respect of the Guaranteed Obligations, any gross-up or make whole payment payable by the Issuer in respect of any such deduction or withholding or any other amount payable by the Issuer in respect of Taxes.

3. **PAYMENTS**

3.1 Following Receipt by MBIA of the Notice of Demand from the Bond Trustee in accordance with Clause 8 (*Notice of Demand*) MBIA will make payments of the Guaranteed Amounts and Recovered Amounts specified in Clause 2.1 that have been properly claimed in such Notice of Demand to the Bond Trustee from its own funds by 11.00 a.m. (London time) on the later of:

3.1.1 the day which is four (4) Business Days following Receipt of a Notice of Demand in accordance with Clause 8 (*Notice of Demand*); and

3.1.2 the day on which the Guaranteed Amounts are Due for Payment or, if that is not a Business Day, on the next succeeding Business Day.

3.2 Payments due under this Financial Guarantee will be satisfied by payment to the person specified in the relevant Notice of Demand in the Relevant Currency by credit to a Relevant Currency account at a bank in London, England, as specified in the Notice of Demand and payment to such person will discharge the obligations of MBIA under this Financial Guarantee to the extent of such payment, whether or not funds are properly applied by such person.

3.3 Once payment of any Guaranteed Amounts or Recovered Amounts have been made to the person specified in the Notice of Demand, MBIA will have no further obligation in respect of such Guaranteed Amounts or Recovered Amounts.

3.4 Nothing in this Financial Guarantee will oblige MBIA to make payments in respect of the Guaranteed Obligations:

3.4.1 earlier than any date on which such payments are Due for Payment; or

3.4.2 which would be greater than the Principal of such part of the Guaranteed Obligations (plus accrued but unpaid interest) as adjusted for indexation in accordance with the Conditions, if applicable.

4. **SUBROGATION**

MBIA will be fully and automatically subrogated to the Holders' and the Bond Trustee's rights in respect of the Guaranteed Obligations to the fullest extent permitted under applicable law to the extent of any payment made by or on behalf of MBIA under this Financial Guarantee.

5. **WAIVER OF DEFENCES**

5.1 The obligations of MBIA under this Financial Guarantee will continue and will not be terminable other than in accordance with Clause 14 (*Termination*) notwithstanding failure to receive payment of the Financial Guarantee Fee or any other fee due in respect of this Financial Guarantee. The Financial Guarantee Fee is not refundable for any reason including payment, or provision being made for payment, prior to the maturity of the Guaranteed Notes.

5.2 Notwithstanding that this Financial Guarantee is a guarantee and not a contract of insurance, neither the obligations of MBIA contained in this Financial Guarantee nor the rights, powers and remedies conferred in respect of MBIA upon the Bond Trustee by this Financial Guarantee or by law shall be discharged, impaired or otherwise affected by:

5.2.1 the winding-up, dissolution, administration or reorganisation of the Issuer or any other person under any applicable law or any change in the status, function, control or ownership of the Issuer or any other person;

5.2.2 any lack of validity or enforceability with respect to the Guaranteed Obligations or the Bond Trust Deed;

5.2.3 any time or other indulgence being granted or agreed to be granted to the Issuer in respect of any of the Guaranteed Obligations or the Bond Trust Deed;

5.2.4 any amendment to, or any variation, waiver or release, with respect to the Guaranteed Obligations or the Bond Trust Deed;

5.2.5 any failure to realise or fully to realise the value of, or any release, discharge, exchange or substitution of, any security taken in respect of the Guaranteed Obligations;

5.2.6 any defence of fraud (including fraud on the part of any agent for the Bond Trustee but excluding fraud by the Bond Trustee) or any defence based on misrepresentation, breach of warranty or non-disclosure of information by any person whether acquired directly, by assignment, by subrogation, or otherwise, to the extent such rights and defences may be available to MBIA to avoid payment of its obligations under this Financial Guarantee; or

5.2.7 any other act, event or omission (other than the failure to deliver a Notice of Demand in accordance with Clause 8 (*Notice of Demand*)) which, but for this Clause 5.2, might operate to discharge, impair or otherwise affect any of the obligations of MBIA contained in this Deed or any of the rights, powers or remedies conferred upon the Bond Trustee and the Holders by the Conditions, the Bond Trust Deed, the Financial Guarantee or by law.

5.3 No warranties are given and nothing in this Financial Guarantee is intended to constitute a warranty or a condition precedent to payment under the Financial Guarantee other than Receipt of a Notice of Demand in accordance with Clause 8 (*Notice of Demand*) below.

5.4 The provisions and waivers set out in Clauses 5.1 to 5.3 above will prevent MBIA from refusing payment of any properly presented claim under this Financial Guarantee but will not, and nothing in this Financial Guarantee will be construed in any way to limit or otherwise affect MBIA's right to pursue recovery or claims (based on contractual or other rights, including such rights resulting from the Bond Trustee's or such other person's fraud, negligence or (subject, in the case of the Bond Trustee only, to any limitation of liability set out in the terms of such agreement) breach of any agreement to which it is a party) for reimbursement against any person for any liabilities, losses, damages, costs and expenses incurred by MBIA after MBIA has made payment in full on the relevant Payment Date of the Guaranteed Obligations.

6. WITHHOLDING AND DEDUCTIONS

6.1 Payments of Guaranteed Amounts and Recovered Amounts by MBIA will be made without withholding or deduction for, or on account of, any present or future Taxes, unless the withholding or deduction of such Taxes is required by law or regulation or administrative practice of any jurisdiction. If any such withholding or deduction is required, MBIA will pay the Guaranteed Amounts and Recovered Amounts net of such withholding or deduction and will account to the appropriate tax authority for the amount required to be withheld or deducted (the "**MBIA Additional Amounts**").

6.2 For the avoidance of doubt, all payments of Guaranteed Amounts and Recovered Amounts by MBIA will be made subject to any other withholding or deduction required by law, regulation or administrative practice in any jurisdiction to which MBIA is subject or in or through which any payment is made by MBIA.

7. ACCELERATION

7.1 At any time or from time to time following Acceleration, MBIA may decide, in its absolute discretion, to make a full or partial Accelerated Payment under this Financial Guarantee without the need for MBIA to have Received and irrespective of whether MBIA shall have Received a Notice of Demand.

7.2 Any Accelerated Payment will be communicated in writing by MBIA to the Bond Trustee without the need for Receipt of a Notice of Demand, and it will be made to the account specified by the Bond Trustee from time to time on not less than 10 Business Days notice. Any such Accelerated Payment shall be considered a payment by MBIA under this Financial Guarantee for all purposes.

7.3 All payments of a partial Accelerated Payment by MBIA under this Financial Guarantee shall be applied as follows:

7.3.1 to pay the Interest accrued but unpaid on the Principal of such part of the Accelerated Payment; and

7.3.2 to reduce each amount of Principal on a *pro rata* basis, with a corresponding reduction of each amount of the Interest.

8. **NOTICE OF DEMAND**

8.1 Payments of Guaranteed Amounts will only be made after Receipt of a validly completed Notice of Demand signed by the Bond Trustee.

8.2 Notices of Demand must be given by the Bond Trustee and delivered by registered mail or personally to the address set out in the Notice of Demand, or such other address as MBIA may notify in writing to the Bond Trustee.

8.3 If any Notice of Demand is not in the proper form or is not properly completed, executed or delivered, it will be deemed not to have been Received by MBIA.

8.4 Any Notice of Demand in respect of a Recovered Amount will not be deemed properly completed unless, among other things, it is accompanied by:

8.4.1 a certified copy of the Order relating to the Recovered Amount;

8.4.2 a certificate of the Bond Trustee that the Order has been entered and is not subject to any stay and specifying the Guaranteed Amounts that are Recovered Amounts; and

8.4.3 an assignment duly executed by the Bond Trustee, irrevocably assigning to MBIA all rights and claims of the Bond Trustee (subject to the provisions of the Bond Trust Deed) relating to or arising out of such Recovered Amounts against the estate of the Issuer or otherwise with respect to such Preference.

8.5 MBIA will promptly advise the Bond Trustee if a Notice of Demand has not been properly completed, executed or delivered and the Bond Trustee may submit an amended Notice of Demand to MBIA.

9. APPOINTMENT OF FISCAL AGENT

9.1 At any time during the term of this Financial Guarantee MBIA may appoint a fiscal agent (the "**Fiscal Agent**") by written notice to the Bond Trustee at the notice address specified in the Bond Trust Deed specifying the name and notice address of the Fiscal Agent, which Fiscal Agent will be situated in London. From and after the date of receipt of such notice by the Bond Trustee:

9.1.1 copies of all notices including the Notice of Demand and other documents required to be delivered to MBIA pursuant to this Financial Guarantee must be simultaneously delivered to the Fiscal Agent and to MBIA and will not be deemed to be Received until they are Received by both the Fiscal Agent and MBIA; and

9.1.2 all payments required to be made by MBIA under this Financial Guarantee will be made directly by MBIA or by the Fiscal Agent on behalf of MBIA, provided, however, that payment by MBIA to the Fiscal Agent will not discharge MBIA's obligations in respect of the Guaranteed Amounts. The Fiscal Agent is the agent of MBIA only and the Fiscal Agent will not be liable to the Bond Trustee or any Holder for any acts by MBIA or any failure by MBIA to deposit, or cause to be deposited, sufficient funds to make payments under this Financial Guarantee.

10. ASSIGNMENT AND TRANSFER

The rights and obligations of MBIA under this Financial Guarantee may be assigned and/or transferred (as the case may be) to any Affiliate of MBIA without the consent of the Bond Trustee or the Holders provided that:

10.1.1 No FG Event of Default (as defined in the Master Definitions Agreement) has occurred and is continuing at the time of such assignment or transfer;

10.1.2 at the time of assignment or transfer, MBIA or such assignee or transferee delivers to the Bond Trustee written confirmation from any two rating agencies then rating the Bonds that, at the time of such assignment or transfer, the financial strength of such assignee or transferee is rated at least equal to the financial strength of MBIA at that time and there is no downgrade to the then current rating of the Bonds by reason only of such assignment or transfer; and

10.1.3 MBIA or such assignee or transferee delivers to the Bond Trustee written notice of any such assignment or transfer and such assignee or transferee assumes the obligations of MBIA under the Financial Guarantee and accedes to the relevant Transaction Documents whereupon, without further action, MBIA will be released from its obligations under this Financial Guarantee.

11. REDENOMINATION

The obligations of MBIA under this Financial Guarantee will not be affected by any redenomination of the Guaranteed Obligations into euro pursuant to Condition 19 (*Redenomination*) of the Bonds save that, following such redenomination, payments of Guaranteed Amounts hereunder shall be made in euro.

12. THIRD PARTY RIGHTS

Any rights which any person (other than MBIA as issuer of this Financial Guarantee and the Bond Trustee as beneficiary of this Financial Guarantee) may otherwise have to enforce any term or condition of this Financial Guarantee pursuant to the Contracts (Rights of Third Parties) Act 1999 are hereby expressly excluded.

13. ENTIRE AGREEMENT

This Financial Guarantee (including the Schedule hereto) constitutes the entire agreement between MBIA and the Bond Trustee in relation to MBIA's obligation to make payments to the Bond Trustee in respect of Guaranteed Amounts and Recovered Amounts and supersedes and replaces any previous agreement or understanding that may have existed between MBIA and the Bond Trustee in relation to such payments.

14. TERMINATION

14.1 This Financial Guarantee will terminate on the date falling two years and one day after the earlier of:

14.1.1 the last Payment Date; and

14.1.2 payment in full of the Guaranteed Obligations

(such date being the "**Termination Date**").

14.2 After the Termination Date, MBIA will cease to be liable in respect of any further demand made in respect of the Guaranteed Obligations.

15. GOVERNING LAW AND JURISDICTION

15.1 Governing Law

This Financial Guarantee and all matters arising from or connected with it shall be governed by and construed in accordance with English law.

15.2 Jurisdiction

15.2.1 The courts of England have exclusive jurisdiction to settle any dispute arising from or connected with this Financial Guarantee (a "**Dispute**"), including a dispute regarding the existence, validity or termination of this Financial Guarantee or the consequences of its nullity.

15.2.2 The parties agree that the courts of England are the most appropriate and convenient courts to settle any Dispute and, accordingly, that they will not argue to the contrary.

16. NO AMENDMENTS

This Deed may only be amended, modified or terminated in writing signed by each party to this Deed.

IN WITNESS WHEREOF this Financial Guarantee has been executed and made effective as a deed by MBIA on the day and year first set out above.

EXECUTION PAGE

EXECUTION PAGE

Executed as a Deed on behalf of
MBIA UK INSURANCE LIMITED

____
Director

____
Director/Secretary

Schedule
Form of Notice of Demand

MBIA UK Insurance Limited
1 Great St Helen's
2nd Floor
London EC3A 6HX

Telephone: 00 44 20 7920 6363
Fax: 00 44 20 7588 3393
Attention: The Director

The undersigned, a duly authorised officer of Deutsche Trustee Company Limited or any additional or successor trustee appointee pursuant to the terms of the Bond Trust Deed (the "**Bond Trustee**"), hereby certifies to MBIA UK Insurance Limited ("**MBIA**"), with reference to Financial Guarantee No. UK [•] (the "**Financial Guarantee**") issued by MBIA in respect of the payment obligations of Southern Water Services (Finance) Limited (the "**Issuer**") in respect of each amount of Principal and Interest owing by the Issuer and outstanding pursuant to the [Issuer's Sub-Class [•] £//$ [•] [•]% Floating Rate/[•]%cent. Index-Linked] Guaranteed Class A Wrapped Bonds due [•]:

1. The Bond Trustee is the trustee under the Bond Trust Deed for the Holders.

2. The Bond Trustee has been notified by the Principal Paying Agent that the deficiency in respect of Guaranteed Amounts which are Due for Payment on [insert Payment Date] will be [*insert applicable amount*] (the "**Shortfall**")[3]/Recovered Amounts recovered from the [Bond Trustee/Holder] on [*insert date*] amount to [*insert applicable amount*] (the "**Shortfall**")[4].

3. The Bond Trustee is making a claim under the Financial Guarantee for the Shortfall to be applied in or towards the payment of [Guaranteed Amounts which are Due for Payment[5]/Recovered Amounts[6]]. No amount claimed hereunder is in excess of the amount properly payable by MBIA under this Financial Guarantee.

4. The Bond Trustee agrees that, following payment of funds by or on behalf of MBIA to the Bond Trustee (if applicable), it will procure that:

4.1 it holds such amounts on trust in favour of the Holders and will apply or procure the application of such amounts directly to the payment of [Guaranteed Amounts which are

[3] Insert if demand relates to non-payment by the Issuer (i.e. demand relates to Guaranteed Amounts).
[4] Insert if demand relates to Recovered Amounts.
[5] Insert if demand relates to non-payment by the Issuer (i.e. demand relates to Guaranteed Amounts).
[6] Insert if demand relates to Recovered Amounts.

Due for Payment and which have not been paid by reason of Nonpayment[7]/Recovered Amounts[8]];

4.2 such funds are not applied for any other purpose and any funds not needed for such purpose will be immediately returned to MBIA;

4.3 such funds are not co mingled with other funds held by the Bond Trustee; and

4.4 a record of payments with respect to each Guaranteed Obligation and the corresponding claim on the Financial Guarantee and the proceeds thereof is maintained by the Principal Paying Agent in accordance with the terms of the Agency Agreement.

5. Payment will be made in the Relevant Currency by credit to the designated Relevant Currency account of the [*insert payee*] at [*insert account details*] with [*insert bank details*] in the Principal Financial Centre.

6. The Bond Trustee acknowledges that the Financial Guarantee and the Bond Trust Deed provide that, effective upon payment by or on behalf of MBIA of the amount claimed hereunder, MBIA shall be fully and automatically subrogated to the Holders' and the Bond Trustee's rights in respect of the Guaranteed Obligations to the fullest extent permitted by applicable law to the extent of any payment made by or on behalf of MBIA under this Financial Guarantee.

7. The Bond Trustee hereby assigns to MBIA all rights of the Bond Trustee to receive any payment of each Guaranteed Amount paid by or on behalf of MBIA under the Financial Guarantee from the Issuer in respect of the Bonds. The foregoing assignment is in addition to, and not in limitation of, rights of subrogation otherwise available to MBIA in respect of such rights. The Bond Trustee shall, at the request and expense of MBIA, take such action and deliver such instruments as may be reasonably requested or required by MBIA to give effect to, or further evidence, the purpose or provisions of this paragraph 7.

8. [Pursuant to Clause 8.4 of the Financial Guarantee, the following documents are attached:

8.1 certified copy of the Order relating to the Recovered Amounts;

8.2 the Bond Trustee's Certificate that the Order has been entered and is not subject to any stay; and

8.3 a duly executed assignment irrevocably assigning to MBIA all rights and claims of the Bond Trustee (subject to the provisions of the Bond Trust Deed) relating to or arising out

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7 Insert if demand relates to non-payment by the Issuer (i.e. demand relates to Guaranteed Amounts).

8 Insert if demand relates to Recovered Amounts.

of such Recovered Amounts against the estate of the Issuer or otherwise with respect to such Preference][9].

9. Unless the context otherwise requires, capitalised terms used in this Notice of Demand and not defined herein will have the meanings set out in the Financial Guarantee.

This Notice of Demand will be revoked in whole or in part (as appropriate) by written notice by the Bond Trustee to MBIA at any time prior to 10.00 a.m. (London time) on the second Business Day prior to the date specified above on which [Guaranteed Amounts are Due for Payment][10]/Recovered Amounts are due for payment[11]] if and only to the extent that moneys are actually received in respect of all or part of the Guaranteed Obligations prior to such time from a source other than MBIA.

This Notice of Demand will be governed by and construed in accordance with English law.

IN WITNESS WHEREOF the Bond Trustee has executed and delivered this Notice of Demand on the [*insert date*] day of [*insert date*].

DEUTSCHE TRUSTEE COMPANY LIMITED

By: ____________________________

Title: ____________________________

9 Insert if demand relates to Recovered Amounts.
10 Insert if demand relates to non-payment by the Issuer (i.e. demand relates to Guaranteed Amounts).
11 Insert if demand relates to Recovered Amounts.

CHAPTER 11
DESCRIPTION OF HEDGE COUNTERPARTIES

THE ROYAL BANK OF SCOTLAND PLC

The Royal Bank of Scotland Group plc (the "**Group**") is the holding company of one of the world's largest banking and financial services groups, with a market capitalisation of £56.8 billion at 30 June 2006. Headquartered in Edinburgh, the Group operates in the UK, the US and internationally through its two principal subsidiaries, The Royal Bank of Scotland plc ("**RBS**") and National Westminster Bank Plc ("**NatWest**"). Both RBS and NatWest are major UK clearing banks whose origins go back over 275 years. The Group has a large and diversified customer base and provides a wide range of products and services to personal, commercial and large corporate and institutional customers.

The Group's operations are conducted principally through RBS and its subsidiaries (including NatWest) other than the general insurance business (primarily Direct Line Group and Churchill Insurance).

The Group had total assets of £839.3 billion and shareholders' equity of £37.4 billion at 30 June 2006. The Group is strongly capitalised with a total capital ratio of 11.9 per cent. and tier 1 capital ratio of 7.6 per cent as at 30 June 2006.

The short-term unsecured and unguaranteed debt obligations of RBS are currently rated A-1+ by S&P, P-1 by Moody's and F1+ by Fitch. The long-term senior unsecured and unguaranteed debt obligations of RBS are currently rated AA by S&P, Aa1 by Moody's and AA+ by Fitch.

In its capacity as Hedge Counterparty, RBS will be acting through its branch at 135 Bishopsgate, London, EC2M 3UR.

The information contained herein with respect to RBS and the Group relates to and has been obtained from it. Delivery of this Prospectus shall not create any implication that there has been no change in the affairs of RBS or the Group since the date hereof, or that the information contained or referred to herein is correct as of any time subsequent to its date.

CITIBANK, N.A., LONDON BRANCH

Citibank, N.A. ("**Citibank**") was originally organised on 16 June 1812, and Citibank now is a national banking association organised under the National Bank Act of 1864 of the United States. Citibank is an indirect wholly-owned subsidiary of Citigroup Inc. ("**Citigroup**"), a diversified global financial services holding company incorporated in Delaware. As of 30 June 2006, the total assets of Citibank and its consolidated subsidiaries represented approximately 48 per cent. of the total assets of Citigroup and its consolidated subsidiaries.

Citibank is a commercial bank that, along with its subsidiaries and affiliates, offers a wide range of banking and trust services to its customers throughout the United States and the world.

Citibank, N.A., London Branch was registered in the United Kingdom as a foreign company in July 1920. The principal offices of the London Branch are located at Citigroup Centre, Canada Square, Canary Wharf, London E14 5LB, England. The London Branch is primarily regulated by The Financial Services Authority and operated in the United Kingdom as a fully authorised commercial banking institution offering a wide range of corporate banking products.

Citibank does not publish auditied financial statements. However, Citigroup publishes audited financial statements that include data relevant to Citibank and its consiolidated subsidiaries, including an audited balance sheet of Citibank and its consolidated subsidiaries. The Consolidated Balance Sheets of Citibank as of 31 December 2005 and as of 31 December 2004 are set forth on page 107 of the Annual Report on Form 10-K of Citigroup and its subsidiaries for the year ended 31 December 2005 and as of 30 June 2006 and 31 December 2005 are set forth on page 86 of the Quarterly Report on Form 10-Q of Citigroup and its subsidiaries for the quarter ended 30 June 2006. Consolidated Balance Sheets of Citibank subsequent to 30 June 2006 will be included in the Form 10-Q's (quarterly) and Form 10-K's (annually) filed by Citigroup with the Securities and Exchange Commission (the "SEC"), which will be filed not later than 40 days after the end of the calendar quarter or 60 days after the end of the calendar year to which the report relates, or on Form 8-K with respect to certain interim events. Copies of such material may be obtained, upon payment of a duplicating fee, by writing to the SEC at 100 F Street, N.E., Washington, D.C. 20549. In addition, such reports of Citigroup are available at the SEC website (http://www.sec.gov).

In addition, Citibank submits quarterly to the U.S. Office of the Comptroller of the Currency (the "Comptroller") certain reports called "Consolidated Reports of Condition and Income for a Bank With Domestic and Foreign Offices" ("Call Reports"). The Call Reports are on file with and publicly available at the Comptroller's offices at 250 E Street, S.W., Washington, D.C. 20219 and are also available on the website of the U.S. Federal Deposit Insurance Corporation of the United States (http://www.fdic.gov). Each Call Report consists of a Balance Sheet, Income Statement, Changes in Equity Capital and other supporting schedules at the end of and for the period to which the report relates. The Call Reports are prepared in accordance with the regulatory instructions issued by the U.S. Federal Financial Institutions Examination Council in the United States. While the Call Reports are supervisory and regulatory documents, not primarily accounting documents, and do not provide a complete range of financial disclosure

about Citibank, the reports provide further information concerning the financial condition and results of operations of Citibank.

The obligations of Citibank, N.A., London Branch under any Hedging Agreement will not be guaranteed by Citigroup or by any other affiliate.

The information contained herein with respect to Citibank and Citigroup and their affiliates relates to and has been obtained from them.

CHAPTER 12
TAX CONSIDERATIONS

The following is a summary of the UK withholding taxation treatment in relation to payments of principal and interest in respect of the Bonds as at the date of this Prospectus. These comments do not deal with other UK tax aspects of acquiring, holding or disposing of Bonds and do not take into consideration any tax implications which may arise on substitution of the Issuer. They relate only to the position of persons who are unconnected with the Issuer and are the absolute beneficial owners of their Bonds and who hold their Bonds as investments. Some sections do not apply to certain classes of taxpayer (such as dealers). Prospective purchasers of Bonds should be aware that the particular terms of issue of any Sub-Class of Bonds as specified in the relevant Final Terms may affect the tax treatment of that and other Sub-Classes or Series of Bonds. This summary as it applies to UK taxation is based upon UK law and HM Revenue and Customs practice as in effect on the date of this Prospectus and is subject to any change in law or practice that may take effect after such date.

Bondholders who may be liable to taxation in respect of their acquisition, holding or disposal of Bonds are advised to consult their professional advisers as to whether they are so liable (and if so under the laws of which jurisdictions) and, if so liable, the basis of determining (including any method of calculating) their liability to tax with respect to the Bonds, since the following comments relate only to certain UK taxation aspects of payments in respect of the Bonds. In particular, Bondholders should be aware that they may be liable to taxation under the laws of other jurisdictions in relation to payments in respect of the Bonds even if such payments may be made without withholding or deduction for or on account of taxation under the laws of the UK.

Prospective purchasers who are in any doubt as to their tax position should consult their professional advisers.

UK Withholding Tax on UK source interest

The Bonds issued by the Issuer will constitute "quoted Eurobonds" provided they are and continue to be listed on a recognised stock exchange within the meaning of Section 841 of the Income and Corporation Taxes act 1988. The London Stock Exchange is a recognised stock exchange for these purposes. Under HM Revenue and Customs published practice, securities will be treated as listed on the London exchange if they are admitted to the Official List by the United Kingdom Listing Authority and are admitted to trading on the London Stock Exchange. HM Revenue and Customs have confirmed that securities that are admitted to trading on the Professional Securities Market satisfy the condition of being admitted to trading on the London Stock Exchange. While the Bonds are and continue to be quoted Eurobonds, payments of interest on the Bonds may be made without withholding or deduction for or on account of United Kingdom income tax.

Subject to "*Payments by the Financial Guarantor*" below, in all cases falling outside the exemption described above, interest on the Bonds will be paid under deduction of United

Kingdom income tax at the lower rate (currently 20 per cent.) subject to such relief as may be available under the provisions of any applicable double taxation treaty or, in certain circumstances; where an exemption for payments between certain United Kingdom companies and partnerships contained in Section 349A Income and Corporation Taxes Act 1988 applies. However, this withholding will not apply if the relevant interest is paid on Bonds with a maturity of less than one year from the date of issue and which are not issued under arrangements the effect of which is to render such Bonds part of a borrowing with a total term of a year or more. If United Kingdom withholding tax is imposed, then the Issuer will not pay additional amounts in respect of the Bonds.

Provision of Information by United Kingdom Paying and Collecting Agents

Bondholders in the United Kingdom (i) paying interest to or receiving interest on behalf of another person who is an individual, or (ii) paying amounts due on redemption of any Bonds which constitute deeply discounted securities as defined in chapter 8 of Part 4 of the Income Tax (Trading and Other Income) Act 2005 to or receiving such amounts on behalf of another person who is an individual, may be required to provide certain information to HM Revenue and Customs regarding the identity of the payee or person entitled to the interest and, in certain circumstances such information may be exchanged with tax authorities in other countries.

For the above purposes, "interest" should be taken, for practical purposes, as including payments made by the Financial Guarantor in respect of interest on Wrapped Bonds.

The provisions referred to above may also apply, in certain circumstances, to payments made on redemption of any Bonds where the amount payable on redemption is greater than the issue price of the Bonds.

Payments by a Financial Guarantor under the Financial Guarantees

If a Financial Guarantor makes any payments in respect of interest on the Wrapped Bonds (or other amounts due under the Wrapped Bonds other than the repayment of amounts subscribed for such Bonds) such payments may be subject to United Kingdom withholding tax at the basic rate (currently 22 per cent) subject to such relief as may be available under the provisions of any applicable double taxation treaty. Such payments by a Financial Guarantor may not be eligible for any of the other exemptions described in "*UK Withholding Tax on UK source interest*" above. If UK withholding tax is imposed, then a Financial Guarantor will not pay any additional amounts under the Financial Guarantees.

Other Rules relating to United Kingdom Withholding Tax

Bonds may be issued at an issue price of less than 100 per cent. of their principal amount. Any discount element on any such Bonds will not be subject to any United Kingdom withholding tax pursuant to the provisions mentioned in "*UK Withholding Tax on UK source interest*" above, but may be subject to reporting requirements as outlined in "*Provision of Information by United Kingdom Paying and Collecting Agents*" above.

Where Bonds are issued with a redemption premium, as opposed to being issued at a discount, then any element of such premium may constitute a payment of interest. Payments of interest are subject to United Kingdom withholding tax and reporting requirements as outlined above.

Where interest has been paid under deduction of United Kingdom income tax, Bondholders who are not resident in the United Kingdom may be able to recover all or part of the tax deducted if there is an appropriate provision in any applicable double taxation treaty.

The references to "interest" above mean "interest" as understood in UK tax law. The statements above do not take any account of any different definitions of "interest" or "principal" which may prevail under any other law or which may be created by the terms and conditions of the Bonds or any related documentation.

The above description of the United Kingdom withholding tax position assumes that there will be no substitution of the Issuer pursuant to Condition 15(d) (*Substitution of the Issue*) of the Bonds and does not consider the tax consequences of any such substitution.

EU Savings Directive

The EU has adopted a Directive regarding the taxation of savings income. The Directive requires Member States to provide to the tax authorities of another Member State details of payments of interest and other similar income paid by a person to an individual in another Member State, except that, Austria, Belgium and Luxembourg will instead impose a withholding system for a transitional period unless during such period they elect otherwise. A number of third countries and territories including Switzerland have adopted similar measures to the EU Directive.

Cayman Islands

The Issuer has been incorporated under the laws of the Cayman Islands as an exempted company and, as such, the Issuer (which was incorporated under the name London 70 Limited) has obtained an undertaking from the Governor in Council of the Cayman Islands substantially in the following form:

"The Tax Concessions Law (1999 Revision) Undertaking as to Tax Concessions

In accordance with Section 6 of the Tax Concessions Law (1999 Revision), the Governor in Council undertakes with London 70 Limited (the "Company"):

(a) that no Law which is hereafter enacted in the islands imposing any tax to be levied on profits, income gains or appreciations shall apply to the Company or its operations; and

(b) in addition, that no tax to be levied on profits, income gains or appreciations or which is in the nature of estate duty or inheritance tax shall be payable:

   (i) on or in respect of the shares debentures or other obligations of the Company; or

   (ii) by way of the withholding in whole or in part of any relevant payment as defined in Section 6(3) the Tax Concessions Law (1999 Revision).

The concessions shall be for a period of twenty years from 4 September 2001.

Governor in Council”

CHAPTER 13
SUBSCRIPTION AND SALE

Dealership Agreement

Bonds may be sold from time to time by the Issuer to any one or more of The Royal Bank of Scotland plc, Citigroup Global Markets Limited, Credit Suisse First Boston (Europe) Limited and Morgan Stanley & Co. International Limited and any other dealer appointed from time to time (the "**Dealers**") or to subscribers from whom subscriptions have been procured by the Dealers, in each case pursuant to the amended and restated dealership agreement dated 13 October 2006 made between, amongst others, SWS, the Issuer, the Co-Arrangers and the Dealers (the "**Dealership Agreement**"). The arrangements under which a particular Sub-Class of Bonds may from time to time be agreed to be sold by the Issuer to, and purchased by, Dealers or subscribers are set out in the Dealership Agreement and the subscription agreements relating to each Sub-Class of Bonds. Any such agreement will, *inter alia*, make provision for the form and terms and conditions of the relevant Bonds, the price at which such Bonds will be purchased by the Dealers or subscribers and the commissions or other agreed deductibles (if any) payable or allowable by the Issuer in respect of such purchase. The Dealership Agreement makes provision for the resignation or termination of appointment of existing Dealers and for the appointment of additional or other Dealers either generally in respect of the Programme or in relation to a particular Series, Class or Sub-Class of Bonds.

In the Dealership Agreement, the Issuer, failing whom SWS, has each agreed to reimburse the Dealers for certain of their expenses in connection with the establishment and maintenance of the Programme and the issue of Bonds under the Dealership Agreement and each of the Obligors has agreed to indemnify the Dealers against certain liabilities incurred by them in connection therewith.

United States of America

The Bonds and any guarantees in respect thereof have not been and will not be registered under the Securities Act and may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons except in certain transactions exempt from the registration requirements of the Securities Act. Terms used in this paragraph have the meaning given to them in Regulation S.

Bearer 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 and regulations thereunder.

Each Dealer has agreed that, except as permitted by the Dealership Agreement, it will not offer, sell or deliver Bonds, (i) as part of their distribution at any time or (ii) otherwise until 40 days after the completion of the distribution of the Bonds comprising the relevant Sub-Class, as certified to the Principal Paying Agent or the Issuer by such Dealer (or, in the case of a sale of a Sub-Class of Bonds to or through more than one Dealer, by each of such Dealers as to the Bonds of such Sub-Class purchased by or through it, in which case the Principal Paying Agent or the

Issuer shall notify each such Dealer when all such Dealers have so certified) within the United States or to, or for the account or benefit of, U.S. persons, and such Dealer will have sent to each Dealer to which it sells 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 meaning given to them in Regulation S.

In addition, until 40 days after the commencement of the offering of Bonds comprising any Sub-Class, any offer or sale of Bonds within the United States by any dealer (whether or not participating in the offering) may violate the registration requirements of the Securities Act.

European Economic Area

In relation to each Member State of the European Economic Area which has implemented the Prospectus Directive (each, a "**Relevant Member State**"), each Dealer has represented, warranted and agreed, and each further Dealer appointed under the Programme will be required to represent, warrant and agree, that with effect from and including the date on which the Prospectus Directive is implemented in that Relevant Member State (the "**Relevant Implementation Date**") it has not made and will not make an offer of Bonds to the public in that Relevant Member State except that it may, with effect from and including the Relevant Implementation Date, make an offer of Bonds to the public in that Relevant Member State:

(a) in (or in Germany, where the offer starts within) the period beginning on the date of publication of a prospectus in relation to those Bonds which has been approved by the competent authority in that Relevant Member State or, where appropriate, approved in another Relevant Member State and notified to the competent authority in that Relevant Member State, all in accordance with the Prospectus Directive and ending on the date which is 12 months after the date of such publication;

(b) at any time to legal entities which are authorised or regulated to operate in the financial markets or, if not so authorised or regulated, whose corporate purpose is solely to invest in securities;

(c) at any time to any legal entity which has two or more of (1) an average of at least 250 employees during the last financial year; (2) a total balance sheet of more than €43,000,000 and (3) an annual net turnover of more than €50,000,000, as shown in its last annual or consolidated accounts; or

(d) at any time in any other circumstances which do not require the publication by the Issuer of a prospectus pursuant to Article 3 of the Prospectus Directive.

For the purposes of this provision, the expression an "offer of Bonds to the public" in relation to any Bonds in any Relevant Member State means the communication in any form and by any means of sufficient information on the terms of the offer and the Bonds to be offered so as to enable an investor to decide to purchase or subscribe the Bonds, as the same may be varied in that Member State by any measure implementing the Prospectus Directive in that Member State and the expression "Prospectus Directive" means Directive 2003/71/EC and includes any relevant implementing measure in each Relevant Member State.

United Kingdom

Each Dealer has represented, warranted and agreed that:

(a) ***No deposit-taking***: in relation to any Bonds having a maturity of less than one year:

(i) it is a person whose ordinary activities involve it in acquiring, holding, managing or disposing of investments (as principal or agent) for the purposes of its business; and

(ii) it has not offered or sold and will not offer or sell any Bonds other than to persons:

(A) whose ordinary activities involve them in acquiring, holding, managing or disposing of investments (as principal or agent) for the purposes of their businesses; or

(B) who it is reasonable to expect will acquire, hold, manage or dispose of investments (as principal or agent) for the purposes of their businesses,

where the issue of the Bonds would otherwise constitute a contravention of Section 19 of the FSMA by the Issuer;

(b) ***Financial Promotion***: it has only communicated or caused to be communicated and will only communicate or cause to be communicated any 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 or sale of any Bonds in circumstances in which section 21(1) of FSMA does not apply to the Issuer; and

(c) ***General Compliance:*** it has complied and will comply with all applicable provisions of FSMA with respect to anything done by it in relation to any Bonds in, from or otherwise involving the United Kingdom.

Cayman Islands

No invitation or solicitation will be made to the public in the Cayman Islands to subscribe for the Bonds.

General

Save for obtaining the approval of the Prospectus by the UK Listing Authority in accordance with Part VI of the FSMA for the Bonds to be admitted to listing on the Official List of the UK Listing Authority and to trading on the Market or the PSM, no action has been or will be taken in any jurisdiction by the Issuer, the other Obligors or the Dealers that would permit a public offering of Bonds, or possession or distribution of the Prospectus or any other offering material, in any jurisdiction where the action for that purpose is required. Each Dealer shall to the best of its knowledge comply with all applicable laws, regulations and directives in each country or jurisdiction in or from which they purchase, offer, sell or deliver Bonds or have in their

possession or distribute the Prospectus or any other offering material, in all cases at their own expense.

The Dealership Agreement provides that the Dealers shall not be bound by any of the restrictions relating to any specific country or jurisdiction (set out above) to the extent that such restrictions shall, as a result of change(s) in the official interpretation, after the date of the Dealership Agreement, of applicable laws and regulations, no longer be applicable but without prejudice to the obligations of the Dealers described in the paragraph above.

Selling restrictions may be supplemented or modified with the agreement of the Issuer. Any such supplement or modification will be set out in the relevant Final Terms (in the case of a supplement or modification relevant only to a particular Sub-Class of Bonds) or (in any other case) in a supplement to this Prospectus.

CHAPTER 14
GENERAL INFORMATION

Authorisation

The establishment of the Programme and the issue of Bonds thereunder have been duly authorised by resolutions of the Board of Directors of the Issuer passed at a meeting of the Board held on 9 June 2003 (as approved by resolutions of SWI dated 9 June 2003) and at a meeting of the Board held on 15 July 2003 (as also approved by resolutions of SWI dated 15 July 2003 and SWS dated 15 July 2003). The update of the Programme and the issue of Bonds thereunder have been duly authorised by resolutions of the Board of Directors of the Issuer passed at a meeting of the Board held on 26 July 2006 (as approved by a written resolution of SWS dated 26 July 2006). The Issuer has obtained or will obtain from time to time all necessary consents, approvals and authorisations in connection with the issue and performance of the Bonds.

The giving of the guarantees by each of SWS, SWSGH and SWSH has been duly authorised by resolutions of the Board of Directors of each of SWS, SWSGH and SWSH, respectively, dated 15 July 2003 and further resolutions of the Board of Directors of each of SWS, SWSGH and SWSH, respectively, dated 26 July 2006.

Listing of Bonds

It is expected that each Sub-Class of Bonds which is to be admitted to the Official List and to trading on the Market or the PSM will be admitted separately as and when issued, subject only to the issue of a Global Bond or Bonds initially representing the Bonds of such Sub-Class. In the case of each Sub-Class of Wrapped Bonds, admission to the Official List and to trading on the Market or the PSM is subject to the issue of the relevant Financial Guarantee by MBIA or any other Financial Guarantor in respect of such Sub-Class. The listing of the Programme in respect of Bonds was granted on 23 July 2003, updated on 26 May 2005 and is expected to be further updated on 13 October 2006.

However, Bonds may also be issued pursuant to the Programme which will not be listed on the Market or the PSM or any other Stock Exchange or which will be listed on such Stock Exchange as the Issuer and the relevant Dealer(s) may agree.

Documents Available

For so long as the Programme remains in effect or any Bonds shall be outstanding, copies of the following documents may (when published) be inspected during normal business hours (in the case of Bearer Bonds) at the specified office of the Principal Paying Agent, (in the case of Registered Bonds) at the specified office of the Registrar and the Transfer Agents and (in all cases) at the registered office of the Bond Trustee:

(i) the Memorandum and Articles of Association of each of the Issuer and the other Obligors;

(ii) MBIA's Articles of Association and By-laws;

(iii) MBIA's memorandum and articles of association;

(iv) the audited financial statements of MBIA for the years ended 31 December 2004 and 31 December 2005;

(v) the audited financial statements of SWS for the years ended 31 March 2005 and 31 March 2006;

(vi) the audited financial statements of SWSGH for the years ended 31 March 2005 and 31 March 2006;

(vii) the audited financial statements of SWSH for the years ended 31 March 2005 and 31 March 2006;

(viii) the audited financial statements of the Issuer for the years ended 31 March 2005 and 31 March 2006;

(ix) the auditors' report from PricewaterhouseCoopers LLP in respect of MBIA's financial statements;

(x) a copy of this Prospectus;

(xi) a copy of an offering circular dated 17 July 2003 in respect of the Programme;

(xii) a copy of an offering circular dated 24 May 2005 in respect of the Programme;

(xiii) each Final Terms relating to Bonds which are admitted to listing, trading and/or quotation by any listing authority, stock exchange and/or quotation system. (In the case of any Bonds which are not admitted to listing, trading and/or quotation by any listing authority, stock exchange and/or quotation system, copies of the relevant Final Terms will only be available for inspection by the relevant Bondholders);

(xiv) each Investors' Report;

(xv) each Financial Guarantee relating to each Sub-Class of Wrapped Bonds issued under the Programme;

(xvi) each G&R Deed;

(xvii) each Issuer/SWS Loan Agreement;

(xviii) the Common Terms Agreement;

(xix) the Registered Office Agreement;

(xx) the Master Definitions Agreement;

(xxi) the STID;

(xxii) the Indemnification Deed;

(xxiii) the Security Agreement;

(xxiv) the Bond Trust Deed;

(xxv) each DSR Liquidity Facility Agreement;

(xxvi) each O&M Reserve Facility Agreement (if any);

(xxvii) each Hedging Agreement;

(xxviii) the Account Bank Agreement;

(xxix) each Subscription Agreement;

(xxx) the Dealership Agreement;

(xxxi) the Agency Agreement;

(xxxii) the Tax Deeds of Covenant;

(xxxiii) the Initial Term Facility Agreement, the Initial RCF Agreement, the Second Revolving Credit Facility Agreement and the Second Artesian Term Facility Agreement;

(xxxiv) the Senior Mezzanine Facility Agreement and the Junior Mezzanine Facility Agreement; and

(xxxv) the SWS/SWSG Loan Agreement and related security document.

This Prospectus can also be viewed on the website of the Regulatory News Service operated by the London Stock Exchange at http://www.londonstockexchange.com/en-gb/pricesnews/marketnews/.

Transparency Directive

Under the terms of the Common Terms Agreement, the Issuer is required, if it is impracticable or unduly burdensome to maintain the admission of all listed Bonds to trading on the London Stock Exchange, to use reasonable endeavours to procure and maintain an alternative listing. The United Kingdom must implement the EU Transparency Directive by 20 January 2007. Following its implementation, if any of the Bonds with a denomination of less than Euro 50,000 (or its equivalent) have been admitted to the Official List and to the Market or any other European Union regulated market, the Issuer may be required to prepare and make public its annual and semi-annual financial reports in accordance with such Directive. If the Issuer considers such obligation to be unduly burdensome, the Issuer may decide to delist the Bonds from the Official List and the Market and to seek an alternative listing of the Bonds on an exchange-regulated market or on a stock exchange outside the European Union.

Clearing Systems

The Bonds have been accepted for clearance through Euroclear and Clearstream, Luxembourg. The appropriate Common Code and ISIN for each Sub-Class of Bonds allocated by Euroclear and Clearstream, Luxembourg will be specified in the applicable Final Terms. If the Bonds are to clear through an additional or alternative clearing system (including Sicovam) the appropriate information will be specified in the applicable Final Terms.

The address of Euroclear is 1 Boulevard du Roi Albert II, B-1210 Brussels, Belgium and the address of Clearstream, Luxembourg is 42 Avenue JF Kennedy L-1855 Luxembourg. The address of any alternative clearing system will be specified in the applicable Final Terms.

Significant or Material Change

There has been no significant change in the financial or trading position and no material adverse change in the financial position or prospects of either the Issuer (or its subsidiaries, if any), SWS (or its subsidiaries), SWSH (or its subsidiaries) or SWSGH (or its subsidiaries), each since 31 March 2006.

There has been no material adverse change in the financial position or prospects of MBIA, since 31 December 2005.

Litigation

Save as disclosed in Chapter 4 ("*Description of the SWS Financing Group*" under "*Litigation/Actions*") of this Prospectus, none of the Issuer or its subsidiaries (if any), SWSGH or its subsidiaries, SWSH or its subsidiaries or SWS or its subsidiaries is or has been involved in any governmental, legal or arbitration proceedings (including any such proceedings which are pending or threatened of which the relevant Obligor is aware) during the 12 months preceding the date of this Prospectus which may have or have had in the recent past significant effects on the financial position or profitability of the Issuer or its subsidiaries (if any), SWSGH or its subsidiaries, SWSH or its subsidiaries or SWS or its subsidiaries, respectively.

MBIA is not and has not been involved in any governmental, legal or arbitration proceedings (including any such proceedings which are pending or threatened of which MBIA is aware) during the 12 months preceding the date of this Prospectus which may have or have had in the recent past significant effect on the financial position or profitability of MBIA.

Availability of Financial Statements

The audited annual financial statements of the Issuer and the audited annual financial statements of SWS will be prepared as of 31 March in each year. The Issuer has not published and does not intend to publish any interim financial statements, but SWS intends to publish semi-annual unaudited financial statements. The unaudited interim financial statements of SWS will be prepared as of 30 September in each year. All future audited annual financial statements (and any published interim financial statements) of SWS and the audited annual financial statements of the Issuer will be available free of charge in accordance with "*Documents Available*" - see paragraphs (v) and (viii) above.

The audited annual financial statements and the unaudited semi-annual financial statements of the MBIA will be prepared as of 31 December and 30 June in each year respectively. All future audited annual financial statements (and any published interim financial statements) of MBIA will be available free of charge in accordance with paragraph "*Documents Available*" above.

Auditors

The auditors of SWS are PricewaterhouseCoopers LLP (as successor entity to PricewaterhouseCoopers and authorised and regulated by the Financial Services Authority for designated investment business), chartered accountants, of 1 Embankment Place, London, WC2N 6RH who have audited SWS' accounts, without qualification, in accordance with generally accepted auditing standards in the United Kingdom for each of the two financial years ended on 31 March 2005 and 31 March 2006.

PricewaterhouseCoopers LLP, chartered accountants, have audited, without qualification, the regulatory financial information of SWS in accordance with generally accepted auditing standards in the United Kingdom for each of the two financial years ended on 31 March 2005 and 31 March 2006.

PricewaterhouseCoopers LLP, chartered accountants, of 1 Embankment Place, London, WC2N 6RH have audited, without qualification, the financial statements of the Issuer in accordance with generally accepted auditing standards in the United Kingdom for each of the two financial years ended on 31 March 2005 and 31 March 2006.

The auditors of SWSGH are PricewaterhouseCoopers LLP, chartered accountants, of 1 Embankment Place, London, WC2N 6RH who have audited SWSGH's accounts, without qualification, in accordance with generally accepted auditing standards in the United Kingdom for each of the two financial years ended on 31 March 2005 and 31 March 2006.

The auditors of SWSH are PricewaterhouseCoopers LLP, chartered accountants, of 1 Embankment Place, London, WC2N 6RH who have audited SWSH's accounts, without qualification, in accordance with generally accepted auditing standards in the United Kingdom for each of the two financial years ended on 31 March 2005 and 31 March 2006.

The auditors of MBIA are PricewaterhouseCoopers LLP of 32 London Bridge Street, London, SE1 9SY who have audited MBIA's accounts, without qualification, in accordance with generally accepted auditing standards in the United Kingdom for each of the two financial years ended on 31 December 2004 and 31 December 2005.

Each report of PricewaterhouseCoopers LLP that is referred to above was produced at the request of the company to which it related.

Bond Trustee's reliance on reports and legal opinions

Certain of the reports of accountants and other experts to be provided in connection with the Programme and/or the issue of Bonds thereunder may be provided on terms whereby they contain a limit on the liability of such accountants or other experts.

Under the terms of the Programme, the Bond Trustee will not necessarily receive a legal opinion in connection with each issue of Bonds.

Legend

Bonds, Receipts, Talons and Coupons appertaining thereto will bear a legend substantially to the following effect: "Any United States person who holds this obligation will be subject to limitations under the United States income tax laws, including the limitations provided in Sections 165(j) and 1287(a) of the Internal Revenue Code." The sections referred to in such legend provide that a United States person who holds a Bond, Coupon, Receipt or Talon generally will not be allowed to deduct any loss realised on the sale, exchange or redemption of such Bond, Coupon, Receipt or Talon and any gain (which might otherwise be characterised as capital gain) recognised on such sale, exchange or redemption will be treated as ordinary income.

Information in respect of the Bonds

The issue price and the amount of the relevant Bonds will be determined, before filing of the relevant Final Terms of each Tranche, based on then prevailing market conditions. The Issuer does not intend to provide any post-issuance information in relation to any issues of Bonds.

Material Contracts

SWS has not entered into contracts outside the ordinary course of the its business, which could result in SWS or any member of its group being under an obligation or entitlement that is material to SWS's ability to meet its obligation to holders of Bonds in respect of the Bonds being issued.

INDEX OF DEFINED TERMS

The following terms are used throughout this Prospectus:

"A Category" means a credit rating of at least A- from S&P, A3 from Moody's or A- from Fitch.

"Acceleration of Liabilities" or **"Acceleration"** means an acceleration of any Secured Liabilities or termination of a commitment (or equivalent action) including:

(a) the delivery of a termination notice from a Finance Lessor or SWS terminating the leasing of Equipment under a Finance Lease;

(b) the delivery of a notice by SWS or a Finance Lessor requesting the prepayment of any Rentals under a Finance Lease;

(c) the early termination of any hedging obligations (whether by reason of an event of default, termination event or other right of early termination) under a Hedging Agreement; or

(d) the taking of any other steps to recover any payment due in respect of any Secured Liabilities, which have matured for repayment and are overdue, by a Secured Creditor or Secured Creditors pursuant to the terms of the applicable Finance Documents and in accordance with the STID,

and **"acceleration"** and **"accelerate"** will be construed accordingly.

"Accession Memorandum" means (a) with respect to the STID, each memorandum entered into or to be entered into pursuant to Clause 2 (*Accession*) or Clause 19 (*Benefit of Deed*) (as applicable) of the STID and (b), with respect to the Bond Trust Deed, a memorandum in substantially the form set out in Schedule 5 to the Bond Trust Deed pursuant to which a Financial Guarantor accedes to the Bond Trust Deed.

"Account" means any bank account of any Obligor.

"Account Bank" means National Westminster Bank Plc or any successor account bank appointed pursuant to the Account Bank Agreement.

"Account Bank Agreement" means the account bank agreement dated the Initial Issue Date (as amended and/or supplemented from time to time) between, among others, the Obligors, the Standstill Cash

Manager, the Account Bank and the Security Trustee.

"Additional Secured Creditor" means any person not already a Secured Creditor which becomes a Secured Creditor pursuant to the provisions of the STID.

"Adjusted Lease Reserve Amount" means, in respect of any Finance Lease and from the commencement of a Standstill in any 12 month period commencing on 1 April in any year, the relevant portion of the Annual Finance Charge for such 12 month period relating to such Finance Lease as calculated pursuant to Paragraph 5.10 of Schedule 12 (*Cash Management*) of the CTA.

"Advance" means any advance or other credit accommodation provided under any Authorised Credit Facility.

"Affiliate" means a Subsidiary or a Holding Company of a person or any other Subsidiary of that Holding Company (other than in any Hedging Agreement when used in relation to a Hedge Counterparty, where **"Affiliate"** has the meaning given to it in that Hedging Agreement).

"Agency Agreement" means the agreement dated the Initial Issue Date (as amended and/or supplemented from time to time) between the Issuer, SWS and the Agents referred to therein under which, among other things, the Principal Paying Agent is appointed as issuing agent, principal paying agent and agent bank for the purposes of the Programme.

"Agent" means the Agent Bank, the Principal Paying Agent, the Registrar, the Transfer Agent and any Paying Agent or any other agent appointed by the Issuer pursuant to the Agency Agreement or a Calculation Agency Agreement.

"Agent Bank" means Deutsche Bank AG London (or any successor thereto) in its capacity as agent bank under the Agency Agreement in respect of the Bonds.

"Ancillary Documents" means the valuations, reports, legal opinions, tax opinions, accountants' reports and the like addressed to or given for the benefit of the Security Trustee, any Obligor or any Secured Creditor in respect of the Security Assets.

"Annual Finance Charge" means, in respect of each 12 month period commencing 1 April in any subsequent year, the aggregate of all interest due or to become due (after taking account of the impact on interest rates of any Hedging Agreements then in place) during that 12 month period on the Class A Debt and the Class B Debt (including, for the avoidance of doubt, all interest due on Class B Debt but not yet payable as a result of the restrictions imposed upon the payment of that

indebtedness contained in the Finance Documents), any Financial Guarantee Fee payable to any Financial Guarantor within that 12 month period, all fees and commissions payable to each Finance Party within that 12 month period and the Lease Reserve Amounts and Adjusted Lease Reserve Amounts falling due in that 12 month period, excluding all indexation of principal, all costs incurred in raising such debt, amortisation of the costs of issue of such debt in that 12 month period and all other costs incurred in connection with the raising of such debt) less all interest received or, in respect of forward-looking ratios, receivable by any member of the SWS Financing Group from a third party during such period (except any interest received or receivable from SWSG under the SWS/SWSG Loan Agreement).

"Applicable Accounting Principles" means accounting principles, standards and practices generally accepted in the United Kingdom as applied from time to time and making such adjustments (if any) as the directors of the relevant company may consider appropriate arising out of changes to applicable accounting principles or otherwise from time to time.

"Appointed Business" means the appointed business of a "relevant undertaker" (as that term is defined by the WIA).

"Artesian" means Artesian Finance plc.

"Artesian II" means Artesian Finance II plc.

"Associate" means:

(a) any person who has a Controlling interest in any member of the SWS Financing Group;

(b) any person who directly or indirectly holds at least 15 per cent. Or more of the voting share capital in any member of the SWS Financing Group;

(c) any person who is Controlled by a member of the SWS Financing Group; or

(d) any person in which a member of the SWS Financing Group holds directly or indirectly at least 15 per cent. or more of the voting share capital,

and in each case, any Affiliate of such person.

"Auditors" means PricewaterhouseCoopers LLP or such other firm of accountants of international repute as may be appointed by SWS in accordance with the CTA as the Auditors for the SWS Financing Group.

"Authorised Credit Facility" means any facility or agreement entered into by the Issuer or SWS for Class A Debt or Class B Debt or Subordinated Debt as permitted by the terms of the CTA or for the issue of Financial Guarantees in relation thereto, the providers of which have acceded to the STID and the CTA, and includes the Liquidity Facilities, the Initial RCF Agreement, the Initial Term Facility Agreement, the Issuer/SWS Loan Agreements, the Bonds, the Hedging Agreements, the Financial Guarantee Fee Letters, the G&R Deeds, the Mezzanine Facility Agreements, the Second Artesian Term Facility Agreement and any other document entered into in connection with the foregoing facilities or agreements or the transactions contemplated in the foregoing facilities or agreements (excluding, however, the Dealership Agreement and the Common Agreements).

"Authorised Credit Provider" means a lender or other provider of credit or financial accommodation under any Authorised Credit Facility and includes each Financial Guarantor for so long as any Financial Guarantee issued by that Financial Guarantor is outstanding, and each Bondholder.

"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;

(c) any other obligations provided that in each case the relevant investment has the Minimum Short-term Rating and is either denominated in pounds sterling or (following the date on which the UK becomes a Participating Member State) euro or has been hedged in accordance with the Hedging Policy; or

(d) any money market funds or equivalent investments which have a rating of at least AAA by S&P or V-1+ by Fitch or Aaa by Moody's.

"Authorised Signatory" means any person who is duly authorised by any Obligor or any Party and in respect of whom a certificate has been provided signed by a director of that Obligor or such Party setting out the name and signature of that person and confirming such person's authority to act.

"Base Cash Flows" means the annual cash flows of the amount of costs netted

off against the amount of receipts and savings in respect of each Relevant Change of Circumstance. Notified Item and relevant disposal of land (as defined in the Licence).

"Base Currency"	means pounds sterling.
"Base Prospectus"	has the meaning given to that term under the "*Important Notice*" above.
"Bearer Bonds"	means those of the Bonds which are in bearer form.
"Bond Trust Deed"	means the bond trust deed dated the Initial Issue Date (and as amended and/or supplemented from time to time) between, among others, the Issuer, the Initial Financial Guarantor and the Bond Trustee, under which Series 1 Bonds and Series 2 Bonds are constituted and any further Bonds will, on issue, be constituted and any bond trust deed supplemental thereto.
"Bond Trustee"	means Deutsche Trustee Company Limited or any successor trustee appointed pursuant to the Bond Trust Deed for and on behalf of the relevant Bondholders.
"Bond Trustee Reserved Matters"	means those matters set out in Part B (*Bond Trustee Reserved Matters*) of Schedule 3 of the STID and Chapter 7 "*Summary of the Financing Agreements*" under "*Security Trust and Intercreditor Deed*" of this Prospectus.
"Bondholders"	means the holders from time to time of the Bonds.
"Bonds"	means the Class A Bonds and/or the Class B Bonds, as the context may require, and "**Bond**" shall be construed accordingly.
"Bridge Facility Agreement"	means the £1,900,000,000 credit agreement dated 8 March 2002, as amended from time to time, between, among others, the Issuer as original borrower and original guarantor and The Royal Bank of Scotland plc as arranger, agent and security trustee under which the relevant lenders made advances that funded the First Aqua Acquisition and funded SWS' working capital requirements and general corporate expenditure. All amounts payable by the SWS Financing Group to the lenders under such credit agreement have been discharged in full.
"BSI"	means the British Standards Institution.
"Business"	means Appointed Business and Permitted Non- Appointed Business or otherwise as permitted under the Finance Documents.

"Business Day" means (other than in any Hedging Agreement where **"Business Day"** has the meaning given to it in that Hedging Agreement):

(a) in relation to any sum payable in euro, a TARGET Settlement Day and a day on which commercial banks and foreign exchange markets settle payments generally in London and each (if any) additional city or cities specified in the relevant Final Terms;

(b) in relation to any sum payable in a currency other than euro, a day on which commercial banks and foreign exchange markets settle payments generally in London, in the principal financial centre of the currency in which such financial indebtedness is denominated (which in the case of a payment in US dollars shall be New York) and in each (if any) additional city or cities specified in the relevant Final Terms; and

(c) in relation to the definition of Lease Calculation Date, a day on which commercial banks and foreign exchange markets settle payments generally in London.

"Calculation Agency Agreement" means, in relation to the Bonds of any Tranche, an agreement in or substantially in the form of Schedule 1 of the Agency Agreement.

"Calculation Agent" means, in relation to any Tranche of Bonds, the person appointed as calculation agent in relation to such Tranche of Bonds by the Issuer pursuant to the provisions of a Calculation Agency Agreement (or any other agreement) and shall include any successor calculation agent appointed in respect of such Tranche of Bonds.

"Calculation Date" means (other than in any Hedging Agreement where **"Calculation Date"** has the meaning given to it in that Hedging Agreement), 31 March and 30 September in each year starting on 30 September 2003 or any other calculation date agreed as a result of a change in the financial year end date of any Obligor.

"Capex Contract" means any agreement pursuant to which SWS outsources any investment, construction works and other Capital Expenditure.

"Capex Reserve Account" means the account of SWS titled "Capex Reserve Account" held at the Account Bank and includes any sub-account relating to that account and any replacement account from time to time.

"Capital Expenditure" means Capital Maintenance Expenditure and any investment expenditure (net of associated grants and contributions) incurred (or, in respect of any future period, forecast to be incurred in the SWS Business Financial Model) relating to increases in capacity or enhancement of service levels, quality or security of supply.

"Capital Maintenance Expenditure" means investment expenditure (net of associated grants and contributions) incurred (or, in respect of any future period, forecast to be incurred in the SWS Business Financial Model) on maintaining base service levels in the Appointed Business but excluding any investment expenditure relating to increases in capacity or enhancement of service levels, quality or security of supply.

"Cash Expenses" means the aggregate of all expenses including capital expenditure incurred by SWS in any period (excluding depreciation, IRC and interest on Financial Indebtedness).

"Cash Manager" means The Royal Bank of Scotland plc during a Standstill Period in its capacity as Standstill Cash Manager under the CTA, or any successor Standstill Cash Manager, and at all other times SWS.

"CC" means the Competition Commission.

"CCD" means expenditure designated under the heading "current cost depreciation" in the financial projections contained in the supplementary report issued by Ofwat detailing the numbers and assumptions specific to SWS in the Director General's most recent Final Determination adjusted as appropriate for any subsequent IDOK and for Out-turn Inflation provided that for the purposes of calculating any financial ratio for any Test Period for which there is no Final Determination, "**CCD**" shall be SWS' good faith, honestly held present estimate of such expenditure for such Test Period.

"CCW" means the Consumer Council for Water.

"Class" means each class of Bonds, the available Classes of Bonds being Class A Wrapped Bonds, Class A Unwrapped Bonds, Class B Wrapped Bonds and Class B Unwrapped Bonds.

"Class A Adjusted ICR" means, in respect of a Test Period, the ratio of Net Cash Flow less the aggregate of CCD and IRC during such Test Period to Class A Debt Interest during such Test Period.

“Class A Average Adjusted ICR” means the sum of the ratios of Net Cash Flow less the aggregate of CCD and IRC to Class A Debt Interest for each of the Test Periods comprised in a Rolling Average Period comprised in a Rolling Average divided by three.

“Class A Bonds” means the Class A Wrapped Bonds and the Class A Unwrapped Bonds.

“Class A Debt” means any financial accommodation that is, for the purposes of the STID, to be treated as Class A Debt and includes all debt outstanding under:

(a) the Class A Wrapped Bonds and the Class A Unwrapped Bonds (if any) issued by the Issuer on or after the Initial Issue Date;

(b) each Initial Authorised Credit Facility Agreement and the Second Artesian Term Facility Agreement;

(c) all Interest Rate Hedging Agreements and the Currency Hedging Agreements in relation to Class A Debt;

(d) the DSR Liquidity Facility and any O&M Reserve Facility entered into after the Initial Issue Date;

(e) the MBIA Financial Guarantee Fee Letter; and

(f) each G&R Deed in respect of Class A Wrapped Debt.

“Class A Debt Instructing Group” or **“Class A DIG”** means a group of representatives (each a **“Class A DIG Representative**”) of Qualifying Class A Debt, comprising of:

(a) in respect of each Sub-Class of Class A Wrapped Bonds or other Class A Wrapped Debt (if no FG Event of Default has occurred and is continuing in respect of the Financial Guarantor of those Bonds), the Financial Guarantor of such Sub-Class of Class A Wrapped Bonds or other Class A Wrapped Debt;

(b) in respect of each Sub-Class of Class A Wrapped Bonds (after an FG Event of Default has occurred and is continuing in respect of the Financial Guarantor of those Bonds) and each Sub-Class of Class A Unwrapped Bonds, the Bond Trustee;

(c) in respect of the Initial RCF Agreement, the Initial RCF Agent and, in respect of the Initial Term Facility, Artesian II and, in respect of the Second Artesian Term Facility, Financial Security Assurance (U.K.) Limited; and

(d) in respect of any other Secured Liabilities of the type referred to in paragraphs (a) to (c) above (excluding liabilities under all Interest Rate Hedging Agreements and under Currency Hedging Agreements in respect of the Class A Debt and under the Liquidity Facilities) or (with the approval of the Majority Creditors) other types of Secured Liabilities that rank *pari passu* with all other Class A Debt, the relevant representative appointed under the terms of the relevant Finance Document and named in the relevant Accession Memorandum or the STID as the Class A DIG Representative.

each of which provides an appropriate indemnity to the Security Trustee each time it votes irrespective of whether it is a Majority Creditor.

"Class A Debt Interest" means, in relation to any Test Period, and without double counting, an amount equal to the aggregate of:

(a) all interest paid, due but unpaid or, in respect of forward-looking ratios, payable, on the Issuer's and/or SWS' obligations under or in connection with all Class A Debt and any Financial Indebtedness which falls under paragraph (e) of Permitted Financial Indebtedness;

(b) all fees paid, due but unpaid or, in respect of forward-looking ratios, payable, to any Financial Guarantor of Class A Debt; and

(c) Adjusted Lease Reserve Amounts or Lease Reserve Amounts paid, due but unpaid or, in respect of forward-looking ratios, payable, on the Issuer's and/or SWS' obligations under and in connection with all Class A Debt,

in each case during such Test Period (after taking account of the impact on interest rates of all related Hedging Agreements then in force) (excluding all indexation of principal, amortisation of the costs of issue of any Class A Debt and/or Class B Debt within such Test Period and all other costs incurred in connection with the raising of such Class A Debt and/or Class B Debt) less all interest received or in respect of forward-looking ratios receivable by any member of the SWS Financing Group from a third party during such period (excluding any interest received or receivable by SWS under the SWS/SWSG Loan Agreement).

“Class A Debt Provider” means a provider of, or Financial Guarantor of, Class A Debt.

“Class A ICR” means, in respect of a Test Period, the ratio of Net Cash Flow for such Test Period to Class A Debt Interest for such Test Period.

“Class A Net Indebtedness” means, as at any date, all the Issuer’s and SWS’ nominal debt outstanding (or, in respect of a future date, forecast to be outstanding) under and in connection with any Class A Debt on such date and the nominal amount of any Financial Indebtedness falling within paragraph (e) of Permitted Financial Indebtedness which is outstanding (or, in respect of a future date, forecast to be outstanding) on such date including all indexation accrued on any such liabilities which are indexed together with any interest due but unpaid up to and including such date (after taking account of the effect of any relevant Interest Rate Hedging Agreements then in force) and less the value of all Authorised Investments and other amounts standing to the credit of any Account (other than an amount equal to the Excluded Insurance Proceeds Amount and an amount equal to the aggregate of any amounts which represent Customer Rebates or Distributions which have been declared but not paid on such date); where such debt is denominated other than in pounds sterling, the nominal amount outstanding will be calculated (I) in respect of debt with associated Currency Hedging Agreements, by reference to the applicable hedge rates specified in the relevant Currency Hedging Agreements; (ii) in respect of debt with no. associated Currency Hedging Agreements, by reference to the Exchange Rate on such date).

“Class A RAR” means, on any Calculation Date, the ratio of Class A Net Indebtedness to RCV as at such Calculation Date or, in the case of any forward-looking ratios for Test Periods ending after such Calculation Date, as at the 31 March falling in such Test Period.

“Class A Required Balance” means, on any Payment Date, the following 12 months’ interest forecast to be due on the Class A Debt.

“Class A Unwrapped Bonds” means the Class A Bonds that do not have the benefit of a guarantee from a Financial Guarantor.

“Class A Unwrapped Debt” means Class A Debt that does not have the benefit of a guarantee from a Financial Guarantor.

“Class A Wrapped Bonds” means the Class A Bonds that have the benefit of a guarantee from a Financial Guarantor.

"Class A Wrapped Debt" means Class A Debt that has the benefit of a guarantee from a Financial Guarantor.

"Class A1 Preference Shares" means the fixed dividend (£40 per share net) cumulative redeemable preference shares 2038 of £1 each in the capital of SWS.

"Class A2 Preference Shares" means the cumulative participating redeemable preference shares 2038 of 1p each in the capital of SWS.

"Class B Bonds" means the Class B Wrapped Bonds and the Class B Unwrapped Bonds.

"Class B Debt" means any financial accommodation that is, for the purposes of the STID, to be treated as Class B Debt and includes all debt outstanding under the Class B Bonds and all Currency Hedging Agreements in relation to Class B Debt.

"Class B Debt Instructing Group" or **"Class B DIG"** means a group of representatives (each a "**Class B DIG Representative**") of Qualifying Class B Debt, comprising of:

(a) in respect of each Sub-Class of Class B Wrapped Bonds (if no FG Event of Default has occurred and is continuing in respect of the Financial Guarantor of those Bonds), the Financial Guarantor of such Sub-Class of Class B Wrapped Bonds;

(b) in respect of each Sub-Class of Class B Wrapped Bonds (after an FG Event of Default has occurred and is continuing in respect of the Financial Guarantor of those Bonds) and each Sub-Class of Class B Unwrapped Bonds, the Bond Trustee;

(c) in respect of any other Secured Liabilities of the type referred to in paragraphs (a) to (b) above (excluding liabilities under the Currency Hedging Agreements in relation to Class B Debt) or (with the approval of the Majority Creditors) other types of Secured Liabilities that rank *pari passu* with all other Class B Debt, the relevant representative appointed under the terms of the relevant Finance Document and named in relevant Accession Memorandum as the Class B DIG Representative,

each of which provides an appropriate indemnity to the Security Trustee each time it votes irrespective of whether it is a Majority Creditor.

"Class B Debt Provider" means any provider of, or Financial Guarantor of, Class B Debt.

"Class B Preference Shares"	means the fixed dividend (£70 per share net) cumulative redeemable preference shares 2038 of £1 each in the capital of SWS.
"Class B Required Balance"	means, on any Payment Date, the next 12 months' interest forecast to be due on the Class B Debt.
"Class B Unwrapped Bonds"	means the Class B Bonds that do not have the benefit of a guarantee from a Financial Guarantor.
"Class B Unwrapped Debt"	means Class B Debt that does not have the benefit of a guarantee from a Financial Guarantor.
"Class B Wrapped Bonds"	means the Class B Bonds that have the benefit of a guarantee from a Financial Guarantor.
"Class B Wrapped Debt"	means Class B Debt that has the benefit of a guarantee from a Financial Guarantor.
"Clearstream, Luxembourg"	means Clearstream Banking, *société anonyme*.
"Co-Arrangers"	means The Royal Bank of Scotland plc and Citigroup Global Markets Limited, the co-arrangers of the Programme.
"Common Agreements"	means the Security Documents, the Bond Trust Deed, the Common Terms Agreement, the Master Definitions Agreement, the Account Bank Agreement, the CP Agreement, the Tax Deeds of Covenants, the SWS/SWSG Loan Agreement, the SWSG Security Agreement, the SWS Preference Share Deed, the Calculation Agency Agreement and any Finance Document to which no Secured Creditor other than the Security Trustee and/or the Issuer and/or any Agent is a party.
"Common Terms Agreement" or **"CTA"**	means the common terms agreement entered into on the Initial Issue Date between, among others, the Obligors, the Initial Financial Guarantor and the Security Trustee, and which contains certain representations and covenants of the Obligors and Events of Default.
"Companies Act 1985"	means the United Kingdom Companies Act 1985.
"Competition Act"	means the United Kingdom Competition Act 1998.
"Competition Commission" or **"CC"**	means the United Kingdom Competition Commission.
"Compliance Certificate"	means a certificate, substantially in the form of Schedule 10 (*Form of Compliance Certificate*) of the CTA in which each of the Issuer and SWS, periodically, provides certain financial statements to the Security Trustee and each Rating Agency as required by the CTA.

"Conditions"	means the terms and conditions of the Bonds set out in the Bond Trust Deed as may from time to time be amended, modified, varied or supplemented in the manner permitted under the STID.
"Construction Output Price Index"	means the index issued by the Department of Trade and Industry, varied from time to time, relating to price levels of new build construction based on a combination of logged values of tender price indices, labour and materials cost indices and on the value of new construction orders in the United Kingdom.
"Contractor"	means any person (being either a single entity, consortium or joint venture) that is a counterparty to an Outsourcing Agreement or Capex Contract.
"Control"	of one person by another person means that the other (whether directly or indirectly and whether by the ownership of share capital, the possession of voting power, contract or otherwise) and whether acting alone or in concert with another or others has the power to appoint and/or remove the majority of the members of the governing body of that person or otherwise controls or has the power to control the affairs and policies of that person (and references to **"Controlled"** and **"Controlling"** shall be construed accordingly).
"Coupon"	means an interest coupon appertaining to a Definitive Bond (other than a Zero Coupon Bond) and includes, where applicable, the Talon(s) appertaining thereto and any replacements for Coupons and Talons issued pursuant to Condition 14 (*Replacement of Bonds, Coupons, Receipts and Talons*).
"Couponholders"	means the several persons who are for the time being holders of the Coupons and includes, where applicable, the Talonholders.
"Court"	means the High Court of England and Wales.
"CP Agreement"	means the conditions precedent agreement dated the Initial Issue Date between, among others, the Bond Trustee, the Security Trustee and the Obligors.
"CSP"	means the Company Stakeholder Plan for SWS employees.
"Currency Hedging Agreement"	means any Hedging Agreement with a Hedge Counterparty in respect of a currency exchange transaction.

"Customer Rebates"	means, in respect of any Financial Year, an amount equal to the difference between the total revenue that is projected by SWS to be raised during such Financial Year on the basis of the announced charges and the revenue that would have accrued if SWS had established prices at the full price cap available to it under the Instrument of Appointment.
"Date Prior"	means, at any time, the date which is one day before the next Periodic Review Effective Date.
"Dealers"	means The Royal Bank of Scotland plc, Citigroup Global Markets Limited, Credit Suisse First Boston (Europe) Limited and. Morgan Stanley & Co. International Limited and any other entity which the Issuer and the other Obligors may appoint as a Dealer and notice of whose appointment has been given to the Principal Paying Agent and the Bond Trustee by the Issuer in accordance with the provisions of the Dealership Agreement but excluding any entity whose appointment has been terminated in accordance with the provisions of the Dealership Agreement and notice of such termination has been given to the Principal Paying Agent and the Bond Trustee by the Issuer in accordance with the provisions of the Dealership Agreement and references to a **"relevant Dealer"** or the **"relevant Dealer(s)"** mean, in relation to any Tranche of Bonds, the Dealer or Dealers with whom the Issuer has agreed the issue of the Bonds of such Tranche and **"Dealer"** means any one of them.
"Dealership Agreement"	means the amended and restated agreement dated on or about the date of this Prospectus between the Issuer, the Obligors and the Dealers named therein (or deemed named therein) concerning the purchase of Bonds to be issued pursuant to the Programme together with any agreement for the time being in force amending, replacing, novating or modifying such agreement and any accession letters and/or agreements supplemental thereto.
"Debt Instructing Group" or **"DIG"**	means the Class A DIG or, following the repayment in full of the Class A Debt, the Class B DIG
"Debt Service Payment Account"	means the account of the Issuer titled "Debt Service Payment Account" held at the Account Bank and includes any sub-account relating to that account and any replacement account from time to time.
"Debt Service Reserve Account"	means the account of the Issuer titled "Debt Service Reserve Account" held at the Account Bank and includes any sub-account relating to that account and any replacement account from time to time.

"Default"	means (a) an Event of Default; (b) a Trigger Event; or (c) a Potential Event of Default.
"Default Situation"	means any period during which there subsists: (a) a Standstill Period; or (b) an Event of Default.
"Definitive Bond"	means a Bearer Bond in definitive form issued or, as the case may require, to be issued by the Issuer in accordance with the provisions of the Dealership Agreement or any other agreement between the Issuer and the relevant Dealer(s), the Agency Agreement and the Bond Trust Deed in exchange for either a Temporary Global Bond or part thereof or a Permanent Global Bond (all as indicated in the applicable Final Terms), such Bearer Bond in definitive form being in the form or substantially in the form set out in Schedule 2, Part C to the Bond Trust Deed and having the Conditions endorsed thereon and having the relevant information supplementing, replacing or modifying the Conditions appearing in the applicable Final Terms endorsed thereon or attached thereto and (except in the case of a Zero Coupon Bond in bearer form) having Coupons and, where appropriate, Receipts and/or Talons attached thereto on issue.
"DEFRA"	means the United Kingdom Department for the Environment, Food and Rural Affairs.
"Determination Date"	means the date which is seven Business Days prior to each Payment Date.
"DETR"	means the Department of the Environment, Transport and the Regions which had responsibility for the Environment prior to DEFRA.
"DGWS" or **"Director General"**	means the Director General of Water Services appointed under Section 1 of the WIA.
"DIG Directions Request"	means a written notice of each DIG Proposal sent by the Security Trustee to the relevant DIG Representatives pursuant to the STID.
"DIG Proposal"	means a proposal pursuant to the STID requiring a Majority Creditor decision in relation to the resignation of the Security Trustee or any vote to terminate or extend Standstill in accordance with the STID.
"DIG Representatives"	means the Class A DIG Representative, or the Class B DIG Representative, or the Senior Mezzanine Facility Agent or the Junior Mezzanine Facility Agent as the context requires,

and **"DIG Representative"** means any of them.

"Directors" means the Board of Directors for the time being of the Issuer or, as the case may be, the relevant Obligor.

"Discharge Date" means the date on which all obligations of the Issuer and SWS under the Finance Documents have been irrevocably satisfied in full and no further obligations are capable of arising under the Finance Documents.

"Distribution" means, other than in respect of payments under the SWS Preference Shares or Subordinated Debt, any payments (including any payments of distributions, dividends, bonus issues, return of capital, fees, interest, principal or other amounts whatsoever) (by way of loan or repayment of any loan or otherwise) (in cash or in kind) to any Associate other than:

(a) payments made to such persons pursuant to arrangements entered into for the provision of management and know-how services and which are entered into on bona fide arm's length terms in the ordinary and usual course of trading to the extent that the aggregate of all such payments does not exceed £10,000,000 (indexed) in any consecutive 12 month period; or

(b) any payments made to such persons pursuant to any Outsourcing Agreements and/or Capex Contracts which were entered into and remain in compliance with the Outsourcing Policy save that if any Outsourcing Agreement and/or Capex Contract should cease to comply with the Outsourcing Policy, all payments thereunder made by SWS shall only be made as Distributions where such non-compliance has remained unremedied for a period in excess of 365 days from the date on which SWS became aware of such non-compliance; or

(c) payments made to such persons pursuant to arrangements entered into on terms that are not bona fide and arm's length in the ordinary and usual course of trading to the extent that the aggregate of all such payments does not exceed £500,000 (indexed) in any consecutive 12 month period; or

(d) payments to The Royal Bank of Scotland plc under or in relation to any Authorised Credit Facility, the Account Bank Agreement or the CTA or in relation to the making by SWS or the Issuer of any

Authorised Investments.

"DSR Liquidity Facility"	means a debt service reserve liquidity facility made available under a Liquidity Facility Agreement.
"DSR Liquidity Facility Agreement"	means any agreement establishing a DSR Liquidity Facility.
"DSR Liquidity Facility Provider"	means The Royal Bank of Scotland plc, or any other lender under a DSR Liquidity Facility Agreement.
"Dual Currency Bonds"	means a Bond in respect of which the amount payable (whether in respect of principal or interest and whether at maturity or otherwise) will be made in such currencies, and based on such rates of exchange, as the Issuer and the relevant Dealer may agree.
"DWI"	means the United Kingdom Drinking Water Inspectorate.
"EA"	means the United Kingdom Environment Agency.
"Early Redemption Amount"	has the meaning, in relation to a Sub-Class of Bonds, given to such term in the Conditions relating to such Sub-Class of Bonds.
"EIN Signatories"	means the DIG Representatives representing 66⅔ per cent. or more of the aggregate Outstanding Principal Amount of the Qualifying Class A Debt (or following the repayment in full of the Class A Debt, the Qualifying Class B Debt) after excluding the Qualifying Debt in respect of which the Bond Trustee is the DIG Representative and in respect of which the Bond Trustee in its absolute discretion has not voted.
"Emergency"	means the disruption of the normal service of the provision of water or wastewater services which is treated as an emergency under SWS' policies, standards and procedures for emergency planning manual (EMPROC) (as amended from time to time).
"Emergency Instruction Notice"	means a notice, setting out the written instructions of the EIN Signatories given to the Security Trustee after (in the case of a STID Proposal) the date specified in the STID Directions Request, being not less than 10 Business Days or (in the case of a DIG Proposal) the date specified in the DIG Directions Request being not less than five Business Days after the date that the STID Directions Request or DIG Directions Request (as applicable) is deemed to be given in accordance with Clause 17.3 (*Effectiveness*) of the Common Terms Agreement.
"Emergency Instruction Procedure"	means an emergency instruction procedure provided for in the Intercreditor Arrangements, subject to Entrenched Rights and Reserved Matters, to cater for circumstances when a

Default Situation is subsisting, and certain decisions and instructions may be required in a timeframe which does not allow the Bond Trustee to convene Bondholder meetings.

"Enforcement Action" means any step (other than the exercise of any rights of inspection of any asset or other immaterial actions taken under any Finance Lease) that a Secured Creditor is entitled to take to enforce its rights against an Obligor under a Finance Document following the occurrence of an Event of Default including, the declaration of an Event of Default, the institution of proceedings, the making of a demand for payment under a Guarantee, the making of a demand for cash collateral under a Guarantee or the Acceleration of Liabilities (other than a Permitted Lease Termination or a Permitted Hedge Termination) by a Secured Creditor or Secured Creditors pursuant to the terms of the applicable Finance Documents.

"Enforcement Order" means an enforcement order, a final enforcement order or a provisional enforcement order, each as referred to and defined in the WIA.

"Enterprise Act" means the Enterprise Act 2002.

"Entrenched Rights" means the rights of the Secured Creditors provided by the terms of Clauses 8.3 to 8.9 (inclusive) of the STID and reproduced in Chapter 7 *"Summary of the financing Agreements"* under *"Security Trust and Intercreditor Deed"* of this Prospectus.

"Entrenched Rights or **Reserved Matters Notice"** means a notice sent by a Secured Creditor (or, where applicable, its Secured Creditor Representative) in response to a STID Directions Request certifying that the consent of such Secured Creditor (or, where applicable, its Secured Creditor Representative) to implementation of the STID Proposal, in relation to which the STID Directions Request is given, is required.

"Environmental Approvals" means any permit, licence, consent, approval or other authorisation and the filing of any notification, report or assessment required under any Environmental Law for the operation of the Business conducted on or from the properties owned or used by SWS.

"Environmental Claim" means any claim, proceeding, formal notice or investigation by any person pursuant to any Environmental Law.

"Environmental Law" means any applicable law (including DETR Circular 02/2000) in force in any jurisdiction in which SWS or any of its Subsidiaries or any Joint Venture in which it has an interest conducts business which relates to the pollution or

protection of the environment or harm to or the protection of human health or the health of animals or plants.

"EPA" means the United Kingdom Environmental Protection Act 1990.

"Equipment" means, in relation to a Finance Lease, any items of equipment, plant and/or machinery, system, asset, software licence, Intellectual Property Right, software and any other item leased under that Finance Lease.

"Equivalent Amount" means the amount in question expressed in the terms of the Base Currency, calculated on the basis of the Exchange Rate.

"EU" means the European Union.

"Euro" means the single currency introduced at the start of the third stage of the European Economic and Monetary Union pursuant to the Treaty establishing the European Community, as amended, from time to time.

"Euroclear" means Euroclear Bank S.A./N.V. as operator of the Euroclear System.

"Event of Default" means (other than in any Hedging Agreement when used in relation to a Hedge Counterparty, where **"Event of Default"** has the meaning given to it in that Hedging Agreement) an event specified as such in Schedule 7 of the CTA (*Events of Default*) as more particularly described in Chapter 7 "*Summary of the financing Agreements*" under "*Security Trust and Intercreditor Deed*" of this Prospectus.

"Exchange Rate" means the spot rate at which the Non-Base Currency is converted to the Base Currency as quoted by the Agent Bank as at 11.00a.m.:

(a) for the purposes of Clause 9.3 (*Notice to Secured Creditors of STID Proposal*) and Clause 9.6 (*DIG Directions Request*) of the STID, respectively, on the date that the STID Proposal or DIG Proposal (as applicable) is dated; and

(b) in any other case, on the date as of which calculation of the Equivalent Amount of the Outstanding Principal Amount is required,

and, in each case, as notified by the Agent Bank to the Security Trustee.

"Excluded Accounts" means the Issuer's O&M Reserve Account and Debt Service Reserve Account to the extent the balance standing to the credit of such accounts is attributable to a Standby Drawing under the relevant Liquidity Facility.

"Excluded Agreement" has the meaning set out in the MDA.

"Excluded Insurance Proceeds Amount" means, at any date, the aggregate of all proceeds of insurance received by SWS to cover the capital cost of re-instatement of assets which have not been applied by SWS in accordance with paragraph 6.5 of Schedule 12 (*Cash Management*) to the CTA; provided that if such aggregate is an amount less than £5,000,000 (indexed) then the "**Excluded Insurance Proceeds Amount**" on such date shall be zero;

"Existing Hedging Agreements" means the interest rate transactions entered into by the Issuer with the Initial Hedge Counterparties on or prior to the Initial Issue Date, as amended from time to time.

"Existing DSR Liquidity Facility" means the DSR Liquidity Facility currently made available under the Existing DSR Liquidity Facility Agreement.

"Existing DSR Liquidity Facility Agreement" means the DSR Liquidity Facility Agreement dated 23 July 2003 between, among others, the Issuer and the Existing DSR Liquidity Facility Providers.

"Existing DSR Liquidity Facility Providers" means The Royal Bank of Scotland plc and Barclays Bank plc or their respective successors.

"Extraordinary Resolution" means a resolution passed by a meeting of Bondholders, duly convened and held in accordance with the Bond Trust Deed, by a majority of not less than three-quarters of the votes cast at such meeting.

"Facility Agent" means any facility agent under any Authorised Credit Facility.

"**FG Event of Default**" means (A) in relation to the Initial Financial Guarantor:

(a) any Guaranteed Amount which is Due for Payment (each as defined under the relevant Financial Guarantee) is unpaid by reason of non-payment by the Issuer and is not paid by such Financial Guarantor on the date stipulated in the relevant Financial Guarantee;

(b) such Financial Guarantor disclaims, disaffirms, repudiates and/or challenges the validity of any of its obligations under the relevant Financial Guarantee or seeks to do so;

(c) such Financial Guarantor:

(i) presents any petition, commences any case or takes any proceedings for the winding-up or the appointment of an administrator or receiver (including as administrative receiver or manager), conciliator, trustee, assignee, custodian, sequestrator, Liquidator or similar official under any Bankruptcy Law, of such Financial Guarantor (or as the case may be, of a material part of its property or assets) under any Bankruptcy Law;

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

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

(iv) has a final and non-appealable order, judgment or decree of a court of competent jurisdiction entered against it appointing any conciliator, receiver, administrative receiver, trustee, assignee, custodian, sequestrator, liquidator, administrator or similar official under any Bankruptcy Law (each a "**Custodian**") for such Financial Guarantor or all or any material portion of its property or authorising the taking of its possession by a Custodian of such Financial Guarantor; and

(B) in relation to any other Financial Guarantor, such events as are specified in that Financial Guarantor's G&R Deed or equivalent document and, in relation to Wrapped Bonds, set out in the relevant Final Terms.

For the purpose of this definition, "**Bankruptcy Law**" means articles L260-1 et seq. And L611-1 et seq. of the French Commercial Code, any similar or future federal or state bankruptcy, insolvency, reorganisation, moratorium, rehabilitation, fraudulent conveyance or similar law, statute or regulation of the French Republic or of any other applicable jurisdiction for the relief of debtors.

"**FG Excepted Amounts**" means any additional amounts relating to premium, prepayment or acceleration, accelerated amounts and Subordinated Coupon Amounts.

"**Final Determination**" means the final price determination made by the Director General on a five-yearly basis.

“Final Terms” means the Final Terms issued in relation to each Tranche or Sub-Class of Bonds as a supplement to the Conditions and giving details of the Tranche or Sub-Class.

Finance Documents” means:

(a) the Security Documents;

(b) the Bond Trust Deed;

(c) the Bonds (including the applicable Final Terms);

(d) the Financial Guarantees;

(e) the G&R Deeds;

(f) the Financial Guarantee Fee Letters;

(g) the Finance Lease Documents;

(h) the Hedging Agreements;

(i) the Common Terms Agreement;

(j) the Issuer/SWS Loan Agreements;

(k) the Initial RCF Facility Agreement;

(l) the Second Revolving Credit Facility Agreement;

(m) the Initial Term Facility Agreement;

(n) the Second Artesian Term Facility Agreement;

(o) the Liquidity Facility Agreements;

(p) the Agency Agreement;

(q) the Mezzanine Facility Agreements;

(r) the Master Definitions Agreement;

(s) the Account Bank Agreement;

(t) the CP Agreement;

(u) any other Authorised Credit Facilities;

(v) the Tax Deeds of Covenant;

(w) the Indemnification Deed;

(x) the SWS/SWSG Loan Agreement and any related security document;

(y) SWS Preference Share Deed; and

(z) each agreement or other instrument between SWS or the Issuer (as applicable) and an Additional Secured Creditor designated as a Finance Document by SWS or the Issuer (as applicable), the Security Trustee and such Additional Secured Creditor in the Accession

Memorandum for such Additional Secured Creditor.

"**Finance Lease Documents**" means each Finance Lease together with any related or ancillary documentation.

"**Finance Leases**" means any finance lease entered into by SWS or the Issuer in respect of plant, machinery, software, computer systems or equipment (the counterparty to which has acceded to the terms of the STID and the CTA) permitted to be entered into under the terms of the CTA, each a "**Finance Lease**".

"**Finance Lessors**" means any person entering into a Finance Lease with SWS, as permitted by the CTA and the STID, who accedes to the STID and the CTA as a Finance Lessor (each a "**Finance Lessor**").

"**Finance Party**" means any person providing financial accommodation pursuant to an Authorised Credit Facility including all arrangers, agents and trustees appointed in connection with any such Authorised Credit Facility.

"**Financial Guarantee Fee**" means any fees payable to the Financial Guarantor under a Financial Guarantee Fee Letter.

"**Financial Guarantee Fee Letter**" means any letter or other agreement between a Financial Guarantor and one or more of the Obligors setting the terms on which premia are payable in relation to one or more Financial Guarantees issued or to be issued by that Financial Guarantor and includes the MBIA Financial Guarantee Fee Letter.

"**Financial Guarantees**" means any financial guarantee issued by a Financial Guarantor in respect of any Wrapped Debt and includes the Initial Financial Guarantees and "**Financial Guarantee**" shall be construed accordingly.

"**Financial Guarantor**" means any person, including the Initial Financial Guarantor and MBIA, which provides a financial guarantee, including the Financial Guarantees, in respect of any of the Wrapped Debt, and "**Financial Guarantors**" means all of them if there is more than one at any time.

"**Financial Indebtedness**" means (without double-counting) any indebtedness for or in respect of:

(a) moneys borrowed or raised (whether or not for cash);

(b) any documentary or standby letter of credit facility;

(c) any acceptance credit;

(d) any bond, note, debenture, loan stock or other similar instrument;

(e) any finance or capital lease or hire purchase contract which would, in accordance with Applicable Accounting Principles, be treated as such;

(f) any amount raised pursuant to any issue of shares which are capable of redemption;

(g) receivables sold or discounted (other than on a non-recourse basis to any member of the SWS Financing Group);

(h) the amount of any liability in respect of any advance or deferred purchase agreement if either one of the primary reasons for entering into such agreement is to raise finance or the relevant payment is advanced or deferred for a period in excess of 90 days;

(i) any termination amount due from any member of the SWS Financing Group in respect of any Treasury Transaction that has terminated;

(j) any other transaction (including any forward sale or purchase agreement) which has the commercial effect of a borrowing (other than any trade credit or indemnity granted in the ordinary course of SWS' trading and upon terms usual for such trade);

(k) any counter-indemnity obligation in respect of any guarantee, indemnity, bond, letter of credit or any other instrument issued by a bank or financial institution; and

(l) any guarantee, indemnity or similar assurance against financial loss of any person in respect of any item referred to in paragraphs (a) to (k) above (other than any guarantee or indemnity in respect of obligations owed by one member of the SWS Financing Group to another).

"**Financial Statements**" means, at any time, the financial statements of an Obligor, consolidated where applicable, most recently delivered to the Security Trustee.

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

"**First Aqua Acquisition**" means the Issuer's acquisition of Southern Water (NR) Limited and its subsidiaries (including SWS) from Scottish Power UK plc in April 2002.

"**Fitch**"	means Fitch Ratings Limited and any successor to the rating agency business of Fitch Ratings Limited.
"**Fixed Rate Bond**"	means a Bond on which interest is calculated at a fixed rate payable in arrear on a fixed date or fixed dates in each year and on redemption or on such other dates as may be agreed between the Issuer and the relevant Dealer(s) (as indicated in the applicable Final Terms).
"**Floating Rate Bond**"	means a Bond on which interest is calculated at a floating rate payable in arrear in respect of such period or on such date(s) as may be agreed between the Issuer and the relevant Dealer(s) (as indicated in the applicable Final Terms).
"**Form of Transfer**"	means the form of transfer endorsed on an Individual Bond Certificate in the form or substantially in the form set out in Schedule 3, Part B to the Bond Trust Deed.
"**FSMA**"	means the Financial Services and Markets Act 2000, as amended.
"**G&R Deed**"	means a guarantee and reimbursement deed (or agreement of similar name and effect) between, among others, the Issuer and a Financial Guarantor in connection with a particular Sub-Class of Class A Wrapped Bonds and/or Class B Wrapped Bonds or any other Class A Wrapped Debt.
"**GAAP**"	means Generally Accepted Accounting Principles.
"**Global Bond**"	means a Temporary Global Bond and/or a Permanent Global Bond, as the context may require.
"**Global Bond Certificate**"	means a Registered Bond in global form in the form or substantially in the form set out in Part A of the Third Schedule to the Bond Trust Deed with such modifications (if any) as may be agreed between the Issuer, the Principal Paying Agent, the Bond Trustee and the relevant Dealer(s), together with the copy of each applicable Final Terms annexed thereto, comprising some or all of the Registered Bonds of the same Sub-Class sold outside the United States or to non-U.S. persons in reliance on Regulation S under the Securities Act, issued by the Issuer pursuant to the Dealership Agreement or any other agreement between the Issuer and the relevant Dealers(s) relating to the Programme, the Agency Agreement and the Bond Trust Deed.
"**Good Industry Practice**"	means the standards, practices, methods and procedures as practised in the United Kingdom conforming to all applicable laws and the degree of skill, diligence, prudence and foresight which would reasonably be expected from a skilled and experienced person undertaking all or part of the

Business as the case may be, under the same or similar circumstances having regard to the regulatory pricing allowances and practices in the United Kingdom's regulated water and sewerage industry at the relevant time.

"**Group**" means Southern Water Investments Limited and its Subsidiaries.

"**Guarantee**" means, in relation to each Obligor, the guarantee of such Obligor given by it pursuant to the Security Document to which it is a party.

"**Guarantors**" means SWSH, SWSGH, SWS and the Issuer, each a "**Guarantor**".

"**Hedge Counterparties**" means (i) the Initial Hedge Counterparties and (ii) any counterparty to a Hedging Agreement which is or becomes party to the STID in accordance with the STID and "**Hedge Counterparty**" means any of such parties.

"**Hedging Agreement**" means:

(a) any Treasury Transaction entered or to be entered into by the Issuer with Hedge Counterparties in accordance with the Hedging Policy (the counterparties to which have acceded to the terms of the STID and the CTA and agreed to be bound by the terms of certain provisions of Schedule 8 (*Hedging Policy and Overriding Provisions Relating to Hedging Agreements*) to the CTA); and

(b) any other Treasury Transaction (the counterparties to which have acceded to the terms of the STID and the CTA and agreed to be bound by the terms of certain provisions of Schedule 8 (*Hedging Policy and Overriding Provisions Relating to Hedging Agreements*) to the CTA) designated a Hedging Agreement by the Security Trustee and the Issuer,

(and references to "**Hedging Agreements**" shall be construed accordingly).

"**Hedging Policy**" means the initial hedging policy applicable to SWS and the Issuer set out in Schedule 8 (*Hedging Policy and Overriding Provisions Relating to Hedging Agreements*) of the CTA as such hedging policy may be amended from time to time by agreement between the Security Trustee, the Issuer and, in certain circumstances, the Hedge Counterparties in accordance with the STID.

"**Holding Company**" means a holding company within the meaning of section 736 of the Companies Act 1985.

"**IDOK**"	means an interim determination of K as provided for in Part IV of Condition B of the Licence.
"**Income**"	means any interest, dividends or other income arising from or in respect of an Authorised Investment.
"**Indemnification Deed**"	means the deed so named and entered into on 18 July 2003 between the Obligors, the Initial Financial Guarantor and the Dealers.
"**Independent Review**"	means an independent review resulting from a Trigger Event as set out in Paragraph 3, Part 2 (*Trigger Event Consequences*) of Schedule 6 to the CTA and set out in Chapter 7 "*Summary of the Financing Agreements*" under "*Common Terms Agreement*".
"**Indexed Bond**"	means a bond in respect of which the amount payable in respect of principal and interest is calculated by reference to an index and/or formula as the Issuer and the relevant Dealer(s) may agree (as indicated in the relevant Final Terms).
"**Individual Bond Certificate**"	means a Registered Bond in definitive form issued or, as the case may require, to be issued by the Issuer in accordance with the provisions of the Dealership Agreement or any other agreement between the Issuer and the relevant Dealer(s), the Agency Agreement and the Bond Trust Deed, such Registered Bond in definitive form being in the form or substantially in the form set out in Schedule 3, Part B of the Bond Trust Deed having the relevant information supplementing, replacing or modifying the Conditions appearing in the applicable Final Terms endorsed thereon or attached thereto and having a Form of Transfer endorsed thereon.
"**Initial Authorised Credit Facilities**"	means the Initial RCF and the Initial Term Facility.
"**Initial Authorised Credit Facility Agreements**"	means the Initial RCF Agreement and the Initial Term Facility Agreement.
"**Initial Authorised Credit Facility Arranger**"	means The Royal Bank of Scotland plc, or any successor thereto.
"**Initial Authorised Credit Provider**"	means The Royal Bank of Scotland plc or any successor thereto.
"**Initial Date Representation**"	has the meaning set out in Chapter 7 "*Summary of the Financing Agreements*" under "*Common Terms Agreement — Representations*".

"**Initial Financial Guarantees**"	means the financial guarantees issued by the Initial Financial Guarantor (subject to the satisfaction of certain conditions set out in the CP Agreement) in connection with the Sub-Classes of Class A Wrapped Bonds issued on the Initial Issue Date and the Sub-Classes of Class A Wrapped Bonds issued on 27 May 2005.
"**Initial Financial Guarantor**"	means MBIA Assurance S.A.
"**Initial Hedge Counterparties**"	means The Royal Bank of Scotland plc and Citibank, N.A., London Branch with whom the Issuer has entered into the Initial Hedging Agreements.
"**Initial Hedging Agreements**"	means each Hedging Agreement entered into with the Initial Hedge Counterparties on or before the Initial Issue Date.
"**Initial Issue Date**"	means 23 July 2003.
"**Initial Issuer/SWS Loan Agreement**"	means the loan agreement entered into between the Issuer and SWS on the Initial Issue Date.
"**Initial Mezzanine Facility Providers**"	has the meaning given to that term on page 14 of the Prospectus.
"**Initial RCF**"	means the revolving credit facilities of an aggregate facility amount of £150,000,000 made available to SWS by the Initial RCF Providers on the Initial Issue Date.
"**Initial RCF Agent**"	means The Royal Bank of Scotland plc, or any successor thereto.
"**Initial RCF Agreement**"	means a facility agreement dated the Initial Issue Date, as amended and restated on 26 July 2005, under which the Initial RCF was made available to SWS.
"**Initial RCF Providers**"	means the syndicate of banks which together provide the Initial RCF.
"**Initial Term Facility**"	means the initial term facility made available to the Issuer by the Initial Term Facility Provider on the Initial Issue Date.
"**Initial Term Facility Agreement**"	means a facility agreement under which the Initial Term Facility was made available to the Issuer and includes that facility agreement in the form amended and restated at the time of the novation of such facility agreement to Artesian II.
"**Initial Term Facility Provider**"	means The Royal Bank of Scotland plc, or any successor thereto including, upon novation of the Initial Term Facility Agreement to Artesian II, Artesian II.
"**Insolvency Event**"	means, in respect of any company: (a) the initiation of or consent to Insolvency

Proceedings by such company or any other person or the presentation of a petition or application for the making of an administration order (other than in the case of the Issuer) and, in the opinion of the Security Trustee, such proceedings are not being disputed in good faith with a reasonable prospect of success;

(b) the giving of notice of appointment of an administrator or the making of an administration order or an administrator being appointed in relation to such company;

(c) an encumbrancer (excluding, in relation to the Issuer, the Security Trustee or any receiver) taking possession of the whole or any part of the undertaking or assets of such company;

(d) any distress, execution, attachment or other process being levied or enforced or imposed upon or against the whole or any substantial part of the undertaking or assets of such company (excluding, in relation to the Issuer, by the Security Trustee or any receiver) and such order, appointment, possession or process (as the case may be) not being discharged or otherwise ceasing to apply within 30 days;

(e) the making of an arrangement, composition, scheme of arrangement, reorganisation with or conveyance to or assignment for the creditors of such company generally or the making of an application to a court of competent jurisdiction for protection from the creditors of such company generally;

(f) the passing by such company of an effective resolution or the making of an order by a court of competent jurisdiction for the winding up, liquidation or dissolution of such company (except, in the case of the Issuer, a winding up for the purpose of a merger, reorganisation or amalgamation the terms of which have previously been approved either in writing by the Security Trustee or by an Extraordinary Resolution);

(g) the appointment of an Insolvency Official in relation to such company or in relation to the whole or any substantial part of the undertaking or assets of such company;

(h) save as permitted in the STID, the cessation or suspension of payment of its debts generally or a public announcement by such person of an intention to do so; or

(i) save as provided in the STID, a moratorium is declared in respect of any indebtedness of such person.

"**Insolvency Official**"	means, in connection with any Insolvency Proceedings in relation to a company, a liquidator, provisional liquidator, administrator, Special Administrator, administrative receiver, receiver, manager, nominee, supervisor, trustee, conservator, guardian or other similar official in respect of such company or in respect of all or substantially all of the company's assets or in respect of any arrangement or composition with creditors.
"**Insolvency Proceedings**"	means, in respect of any company, the winding-up, liquidation, dissolution, administration of such company, or any equivalent or analogous proceedings under the law of the jurisdiction in which such company is incorporated or of any jurisdiction in which such company carries on business, including the seeking of liquidation, winding-up, reorganisation, dissolution, administration, arrangement, adjustment, protection or relief of debtors.
"**Instalment Bonds**"	means any Bonds specified as being instalment bonds in the relevant Final Terms.
"**Instructing Group**"	means the Class A DIG or, following repayment in full of the Class A Debt, the Class B DIG or, following repayment of the Class A Debt and the Class B Debt in full, the "Majority Lenders" under the Senior Mezzanine Facility Agreement (as defined therein) and or, following repayment of the Senior Mezzanine Debt in full, the "Majority Lenders" under the Junior Mezzanine Facility Agreement (as defined therein).
"**Instrument of Appointment**" or **"Licence**"	means the instrument of appointment dated August 1989 under sections 11 and 14 of the Water Act 1989 (as in effect on 1 September 1989) under which the Secretary of State for the Environment appointed SWS as a water and sewerage undertaker under that Act for the areas described in the Instrument of Appointment, as modified or amended from time to time.
"**Insurances**"	means, as the context may require, any or all of the insurances described in or taken out pursuant to Schedule 16 (*Insurances*) of the CTA and any other contract or policy of

insurance taken out by an Obligor from time to time, including in each case any future renewal or replacement of any such insurance whether with the same or different insurers and whether on the same or different terms as further defined in Schedule 16 (*Insurances*) of the CTA.

"**Intellectual Property Right**" means all right, title and interest in:

(a) any trade mark, service mark, trade name, logo, patent, invention, design or similar right;

(b) any designs, copyright, semi-conductor topography, database and know-how or intellectual property right; and

(c) all such similar rights which may subsist in any part of the world,

in each case whether registered or not, whether in existence now or in the future, and includes any related application.

"**Intercompany Loan**" means the principal amount of all advances from time to time outstanding under an Issuer/SWS Loan Agreement.

"**Intercreditor Arrangements**" means the arrangements between the Secured Creditors of the SWS Financing Group in the STID summarised in Chapter 7 "*Summary of the Financing Agreements*" under "*Security Trust and Intercreditor Deed*".

"**Interest Commencement Date**" means, in the case of interest-bearing Bonds, the date specified in the applicable Final Terms from (and including) which such Bonds bear interest, which may or may not be the Issue Date.

"**Interest Payment Date**" means any date upon which interest or payments equivalent to interest become payable under the terms of any Authorised Credit Facility.

"**Interest Rate Hedging Agreement**" means a Treasury Transaction to swap interest rates.

"**Investment Grade**" means a rating of at least BBB- by Fitch, Baa3 by Moody's or BBB- by S&P.

"**Investors Report**" means each report produced by SWS and the Issuer to be delivered within 120 days from 31 March or 60 days from 30 September in each year substantially in the form set out in the CTA.

"**IRC**" means the amounts set out under the heading infrastructure renewals charge in the financial projections contained in the supplementary report issued by Ofwat detailing the numbers and assumptions specific to SWS in the Director General's most recent Final Determination adjusted as appropriate for

any subsequent IDOK and for Out-turn Inflation, provided that for the purposes of calculating any financial ratio for any Test Period for which there is no Final Determination, "**IRC**" shall be SWS' good faith, honestly held present estimate of such infrastructure renewals charge for such Test Period.

"**ISDA Master Agreement**" means an agreement in the form of the 1992 or 2002 ISDA Master Agreement (Multi-Currency Cross Border) or any successor thereto published by ISDA unless otherwise agreed by the Security Trustee.

"**Issue Date**" means the date of issue of any Tranche of Bonds or the date upon which all conditions precedent to a utilisation under any other Authorised Credit Facility have been fulfilled or waived and the Issuer makes a utilisation of that facility.

"**Issue Price**" means the price as stated on the relevant Final Terms, generally expressed as a percentage of the nominal amount of the Bonds, at which the Bonds will be issued.

"**Issuer**" means Southern Water Services (Finance) Limited a company incorporated in the Cayman Islands with limited liability under 112331.

"**Issuer/SWS Loan Agreement**" means any loan agreement entered into between the Issuer and SWS, including the Initial Issuer/SWS Loan Agreement, the Second Issuer/SWS Loan Agreement and the Third Issuer/SWS Loan Agreement.

"**Joint Venture**" means any arrangement or agreement for any joint venture, co-operation or partnership pursuant to, required for or conducive to the operation of the Business by SWS but shall exclude any arrangements or framework agreements entered into with a Contractor which are in accordance with and subject to the Outsourcing Policy.

"**Junior Mezzanine Debt**" means the principal amount outstanding of the loan made by the Junior Mezzanine Facility Providers under the Junior Mezzanine Facility Agreement.

"**Junior Mezzanine Facility**" means a credit facility in the amount of £106,000,000 provided by Junior Mezzanine Facility Providers to the Issuer pursuant to the Junior Mezzanine Facility Agreement.

"**Junior Mezzanine Facility Agent**" means The Royal Bank of Scotland plc or any successor thereto as agent under the Junior Mezzanine Facility Agreement.

"**Junior Mezzanine Facility Agreement**" means the £106,000,000 junior mezzanine facility agreement dated the Initial Issue Date between the Issuer, the Junior Mezzanine Facility Agent, the Junior Mezzanine Facility

	Arranger, the Original Junior Mezzanine Facility Provider and the Security Trustee.
"**Junior Mezzanine Facility Arranger**"	means RBEF Limited.
"**Junior Mezzanine Facility Provider**"	means the "Lenders" (as defined in the Junior Mezzanine Facility Agreement).
"**Junior Mezzanine Finance Parties**"	means (a) the Junior Mezzanine Facility Agent; (b) the Junior Mezzanine Facility Arranger; and (c) the Junior Mezzanine Facility Providers.
"**K**"	means the adjustment factor set for each year by the DGWS by which charges made by Regulated Companies for water supply and sewerage services may be increased, decreased or kept constant.
"**K3 Period**"	means the Periodic Review Period that started on 1 April 2000 and ended on 31 March 2005.
"**K4 Period**"	means the Periodic Review Period that started on 1 April 2005.
"**Lead Manager**"	means in relation to any Tranche of Bonds, the person named as the lead manager in the relevant Subscription Agreement.
"**Lease Calculation Cashflow**"	means, in respect of any 12 month period commencing on 1 April in any year, for any Finance Lease, a cashflow statement produced by the relevant Finance Lessor on, or as soon as reasonably practicable after, its Lease Calculation Date occurring prior to the commencement of such 12 month period and in accordance with its terms and the terms of the relevant Accession Memorandum, and using, *inter alia*, for the purposes of calculating the amount shown for each Rental Payment Date falling within the relevant 12 month period under the heading "interest" (or the equivalent thereof (howsoever worded)) in such cashflow statement, a rate of LIBOR, estimated, as at its Lease Calculation Date, by reference to the average of those rates per annum being offered by certain reference banks to prime banks in the London interbank market for entry into 12 month (or such other period as is equal to the relevant Rental Period under such Finance Lease) forward contracts, commencing on each Rental Payment Date arising during the period commencing on such Lease Calculation Date and ending on the last Rental Payment Date to occur during the relevant 12 month period and as agreed between SWS and the relevant Finance Lessor (provided that, where any Finance Lease contains Rentals which are calculated by reference to a fixed rate of

interest, any Lease Calculation Cashflow produced in respect of that Finance Lease shall reflect the actual fixed rate of interest implicit in such Rental calculations), provided that where in respect of any Finance Lease there has been a change of assumption resulting in an increase or decrease in the Rental payable thereunder during any 12 month period commencing on 1 April in any year, the Lease Calculation Cashflow applicable to that Finance Lease for such 12 month period shall also include a cashflow statement, produced as soon as reasonably practicable after the time of recalculating the Rental and in accordance with its terms, and the terms of the relevant Accession Memorandum and using, in such cashflow statement, the same estimated interest rates as were used in preparation of the original cashflow statement prepared on or as soon as reasonably practicable after the Lease Calculation Date applicable to that 12 month period.

"**Lease Calculation Date**" means in respect of any Finance Lease:

(a) the date of the Accession Memorandum executed by the relevant Finance Lessor relating to such Finance Lease; and

(b) the date falling 10 days before the Rental Payment Date immediately preceding the commencement date of the first 12 month period to commence on 1 April immediately after the date referred to in (a) above; and

(c) each yearly anniversary of the date referred to in (b) above,

save that where any date referred to in (a), (b) or (c) is not a Business Day, such date shall be deemed to be the preceding Business Day.

"**Lease Reserve Amount**" means in respect of any Finance Lease in any 12 month period commencing on 1 April in any year, the lower of (i) the aggregate Notional Amount calculated with respect to such Finance Lease; and (ii) the aggregate amount of rental payments payable to the Finance Lessor under such Finance Lease during such 12 month period (inclusive of VAT) (after adding back any additional rentals (inclusive of VAT) payable and deducting any estimated rental rebates (inclusive of any credit for VAT), in each case as determined in accordance with the provisions of the relevant Finance Lease).

"**LIBOR**"	has the meaning given to that term in the relevant Finance Document.
"**Licence**"	means the instrument of appointment dated August 1989 under sections 11 and 14 of the Water Act 1989 (as in effect on 1 September 1989) under which the Secretary of State for the Environment appointed SWS as a water and sewerage undertaker under that Act for the areas described in the Instrument of Appointment, as modified or amended from time to time.
"**Liquidity Facility**"	means a DSR Liquidity Facility or an O&M Reserve Facility made available under a Liquidity Facility Agreement and "**Liquidity Facilities**" means all of them.
"**Liquidity Facility Agent**"	means, in respect of the Existing DSR Liquidity Facility Agreement, The Royal Bank of Scotland plc and, in respect of any other Liquidity Facility Agreement, the Facility Agent under such Liquidity Facility Agreement.
"**Liquidity Facility Agreement**"	means each liquidity facility agreement which has the characteristics set out in Schedule 15 (*DSR Liquidity Facility/O&M Reserve Facility Terms*) of the CTA, as established in connection with each Sub-Class of Bonds issued by or other Authorised Credit Facility provided to the Issuer or SWS or shortfalls in funding for Projected Operating Expenditure or projected Capital Maintenance Expenditure, each counterparty to which has acceded to the terms of the STID and the CTA.
"**Liquidity Facility Provider**"	means any lender from time to time under a Liquidity Facility Agreement that has agreed to be bound by the terms of the STID and the CTA, including the DSR Liquidity Facility Provider(s) and any O&M Reserve Facility Provider(s).
"**Liquidity Facility Requisite Ratings**"	means together the Minimum Short-term Rating from at least two Rating Agencies.
"**London Stock Exchange**"	means The London Stock Exchange plc.
"**Majority Creditors**"	means the Class A DIG Representatives in respect of more than 50 per cent. of the Voted Qualifying Class A Debt or, following the repayment in full of the Class A Debt, the Class B DIG Representatives in respect of more than 50 per cent. of the Voted Qualifying Class B Debt, in each case subject to Clause 8 (*Modifications, Consents and Waivers*) and Clause 9 (*Voting, Instructions and Notification of Outstanding Principal Amount of Qualifying Debt*) of the STID as set out in Chapter 7 "*Summary of the Financing Agreements*".

"Make-Whole Amount" means any amount above par payable on redemption of any Class A Debt or Class B Debt except where such amount is limited to accrued interest.

"Mandatory Cost Rate" means, in relation to any Authorised Credit Facility, the addition to the interest rate payable to compensate that Authorised Credit Provider for the cost of compliance with the requirements of the Bank of England and/or the Financial Services Authority (or, in either case, any other authority which replaces all or any of its functions) in accordance with the formula(e) set out in the relevant Authorised Credit Facility.

"Market" means the London Stock Exchange's Gilt-Edged and Fixed Interest Market.

"Master Definitions Agreement" or **"MDA"** means the master definitions agreement entered into on the Initial Issue Date and amended on 13 October 2006, made between, among others, the Obligors, the Bond Trustee, the Initial Financial Guarantor and the Security Trustee.

"Material Adverse Effect" means the effect of any event or circumstance which is materially adverse, taking into account the timing and availability of any rights or remedies under the WIA or the Instrument of Appointment, to:

(a) the business, property, operations or financial condition of SWS, the Issuer or of the SWS Financing Group as a whole;

(b) the ability of any member of the SWS Financing Group to perform its material obligations under any Finance Document;

(c) the validity or enforceability of any Finance Document or the rights or remedies of any Secured Creditor thereunder; or

(d) the ability of SWS to perform or comply with any of its obligations under the Instrument of Appointment or the WIA.

"Material Agreement" means:

(a) for the purpose of Schedule 2 (*Material Entity Events*) to the CTA and Paragraph 11 (*Material Entity Event*) of Part 1 and Part 3 of Schedule 6 (*Trigger Events*) only:

(i) any Capex Contract (or series of Capex Contracts) with the same Contractor (or its Affiliates) entered into by SWS for the purposes of, or in connection

with, SWS carrying out its Regulated Business, where the NPV at the later of (a) the Initial Issue Date and (b) the date at which it is entered into or amended, supplemented or novated, of the agreed target cost payable by SWS under that Capex Contract (which in each case has not been terminated or expired in accordance with its terms), is, or would be, if such contract was entered into on arm's length terms and for full value, equal to or greater than £25 million (indexed); and/or

(ii) any Outsourcing Agreement (or series of Outsourcing Agreements) entered into with the same Contractor (or its Affiliates) where the annual value of the contracts entered into between SWS and such Contractor (or its Affiliates) (which in each case has not been terminated or expired in accordance with its terms) exceeds (or would exceed if entered into on arms' length terms) 10 per cent. of the Projected Operating Expenditure for the Test Periods in which such contracts are entered into.

(b) except as provided for in (i) above, any Material Capex Agreement and Material O&M Agreement.

"**Material Capex Agreement**" has the meaning given to that term in the Outsourcing Policy.

"**Material Entity Event**" means the events or circumstances set out in Schedule 2 (*Material Entity Events*) to the CTA and described in Chapter 7 "*Summary of the Financing Agreements*" under "*Common Terms Agreement – Material Entity Events*" of this Prospectus.

"**Material O&M Contract**" has the meaning given to that term in the Outsourcing Policy.

"**Maturity Date**" means the date on which a Bond is expressed to be redeemable or any other Authorised Credit Facility is expressed to be repayable in full.

"**MBIA**" means MBIA UK Insurance Limited

"**MBIA Financial Guarantee Fee Letter**" means the Financial Guarantee Fee Letter between the Initial Financial Guarantor and the Issuer relating to the Initial Financial Guarantees.

"**MBIA Information**" means the information contained in Chapter 10 "*MBIA and its Financial Guarantees*" on pages 241 to 270 and in the paragraphs relating to MBIA under the headings "*Significant or Material Change*", "*Litigation*", "*Availability of Financial Statements*" and "*Auditors*", in Chapter 14

"*General Information*" on pages 285 and 286.

"**Member State**"	means a member state of the European Union.
"**Meter Optants**"	means domestic customers who have opted to be charged on the basis of a meter reading rather than by rateable value.
"**Mezzanine Debt**"	means the Senior Mezzanine Debt and the Junior Mezzanine Debt.
"**Mezzanine Facilities**"	means the Senior Mezzanine Facility and the Junior Mezzanine Facility.
"**Mezzanine Facility Agreements**"	means the Senior Mezzanine Facility Agreement and the Junior Mezzanine Facility Agreement.
"**Mezzanine Facility Provider**"	means a Senior Mezzanine Facility Provider and/or a Junior Mezzanine Facility Provider.
"**Mezzanine Finance Parties**"	means the Senior Mezzanine Finance Parties and the Junior Mezzanine Finance Parties.
"**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, "Prime-1"; in the case of S&P, "A-1"; and in the case of Fitch, "F-1".
"**Monthly Payment Amount**"	has the meaning set out in Paragraph 5.9 of Schedule 12 (*Cash Management*) to the Common Terms Agreement, approximately (and subject to adjustment) equal to 1/12th of SWS' Annual Finance Charge for the relevant 12 month period.
"**Moody's**"	means Moody's Investors Service, Limited, or any successor to the rating agency business of Moody's Investors Service, Limited.
"**Moody's Minimum Long-term Rating**"	means in respect of any person, such person's long-term unsecured debt obligations being rated A2 by Moody's.
"**Net Cash Flow**"	means:
	(a) in respect of any historical element of a Test Period, the aggregate of net cash flow from operating activities as shown in the SWS financial statements (after adding back, without double counting, and to the extent that such items are included in net cash flow from operating activities, any exceptional items (other than non-cash exceptional items), any recoverable VAT, any Capital Expenditure and any movement in debtors and/or creditors relating to Capital Expenditure) minus corporation tax paid which shall exclude payments in respect of a Permitted Tax Loss Transaction as part of any

SWS/SWSG Debt Service Distribution, during such Test Period; and

(b) in respect of any forward-looking element of a Test Period, the aggregate of anticipated net cash flow from operating activities (after adding back, without double counting and to the extent that such items are included in the anticipated net cash flow from operating activities, any exceptional items (other than non-cash exceptional items), any recoverable VAT, any Capital Expenditure and any movement in debtors and/or creditors relating to Capital Expenditure in each case anticipated to occur during such Test Period) minus corporation tax which shall exclude payments in respect of a Permitted Tax Loss Transaction as part of any SWS/SWSG Debt Service Distributions anticipated to be paid during such Test Period less any anticipated net cash flow from operating activities of its business other than its Appointed Business and after adding back corporation tax anticipated to be paid as a result of such businesses during such Test Period.

"**New Money Advance**" means any drawing during a Standstill under any Authorised Credit Facility which is not made (or to the extent not made) for the purpose of refinancing a drawing under such Authorised Credit Facility.

"**Non-Appointed Expense**" means any expense incurred in connection with activities other than Appointed Business.

"**Non-Base Currency**" means a currency other than pounds sterling.

"**Notice**" or "**notice**" means, in respect of a notice to be given to Bondholders, a notice validly given pursuant to Condition 17 (Notices).

"**Notified Item**" has the meaning given to such term in Chapter 6 "*Water Regulation*" under "*Interim Determinations of K*".

"**Notional Amount**" means, in respect of any Finance Lease, a sum, certified by any Authorised Signatory of the relevant Finance Lessor on each Lease Calculation Date and using the relevant Lease Calculation Cashflow relating thereto as being, for the succeeding 12 month period commencing on 1 April, the amount shown for each Rental Payment Date falling in that relevant 12 month period under the headings "interest" and "margin" (or any equivalents thereof (howsoever worded)) in such Lease Calculation Cashflow, together with an amount equal to the VAT on such amount at the rate applicable to rentals payable under the relevant Finance

Lease.

"**NPV**"	means, in respect of any amount payable or receivable at a future date, such amount discounted back to the date of calculation on an annual basis at a discount rate of 7.5 per cent.
"**O&M Reserve**"	means the amounts standing to the credit of the O&M Reserve Accounts.
"**O&M Reserve Accounts**"	means the accounts of SWS and/or the Issuer entitled "O&M Reserve Account" held at the Account Bank and includes any sub-account relating to that account and any replacement account from time to time.
"**O&M Reserve Facility**"	means any operation and maintenance reserve liquidity facility made available under a Liquidity Facility Agreement.
"**O&M Reserve Facility Agreement**"	means an agreement establishing an O&M Reserve Facility.
"**O&M Reserve Facility Provider**"	means any provider from time to time of an O&M Reserve Facility.
"**O&M Reserve Required Amount**"	means not less than 10 per cent. of Projected Operating Expenditure and Capital Maintenance Expenditure required for the next succeeding 12 month period as forecast in the SWS Business Financial Model.
"**Obligors**"	means the Issuer, SWS, SWSH and SWSGH and "**Obligor**" means any of them.
"**Official List**"	means the official list of the UKLA.
"**OFT**"	means the Office of Fair Trading in the United Kingdom.
"**Ofwat**"	means The Office of Water Services in England and Wales including its successor office or body.
"**Operating Accounts**"	means each account of SWS with the following titles: SWS Ltd. CAO Income. SWS Ltd. Misc Income, SWS Collections, SWS Ltd. No.2 Refunds, General Payments No.3, and SWS Ltd. Central Account held at the Account Bank and includes any sub-account or sub-accounts relating to that account and any replacement account or accounts from time to time.
"**Order**"	means the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005.
"**Original Junior Mezzanine Facility Provider**"	means Royal Bank Investments Limited.

"**Original Senior Mezzanine Facility provider**" means Royal Bank Investments Limited.

"**Other Parties**" means the Hedge Counterparties, the Liquidity Facility Providers, the Authorised Credit Providers, the Mezzanine Facility Providers, the Agents, the Account Bank, the Standstill Cash Manager and members of the Group (other than the Obligors).

"**Outsourcing Agreement**" means any agreement pursuant to which SWS sub-contracts, tenders or outsources either the day to day operation of its assets, business services and service delivery (including any maintenance expenditure) or acquires technical know-how and access to other Intellectual Property Rights in relation to water and sewerage services that, in the case of any outsourcing SWS could, if not outsourced, perform itself.

"**Outsourcing Policy**" means the outsourcing policy set out in Schedule 9 (*Outsourcing Policy*) to the CTA (as amended or replaced from time to time).

"**Outstanding**" means, in relation to the Bonds of all or any Sub-Class, all the Bonds of such Sub-Class issued other than:

(a) those Bonds which have been redeemed pursuant to the Bond Trust Deed;

(b) those Bonds in respect of which the date (including, where applicable, any deferred date) for redemption in accordance with the Conditions has occurred and the redemption moneys (including all interest payable thereon) have been duly paid to the Bond Trustee or to the Principal Paying Agent in the manner provided in the Agency Agreement (and where appropriate notice to that effect has been given to the relative Bondholders in accordance with Condition 17 (*Notices*)) and remain available for payment against presentation of the relevant Bonds and/or Receipts and/or Coupons;

(c) those Bonds which have been purchased and cancelled in accordance with Condition 8(f) and (h) (*Redemption, Purchase and Cancellation — Cancellation*);

(d) those Bonds which have become void or in respect of which claims have become prescribed, in each case under Condition 13 (*Prescription*);

(e) those mutilated or defaced Bonds which have been surrendered and cancelled and in respect of which

replacements have been issued pursuant to Condition 14 (*Replacement of Bonds, Coupons, Receipts and Talons*);

(f) (for the purpose only of ascertaining the nominal amount of the Bonds outstanding and without prejudice to the status for any other purpose of the relevant Bonds) those Bonds which are alleged to have been lost, stolen or destroyed and in respect of which replacements have been issued pursuant to Condition 14 (*Replacement of Bonds, Coupons, Receipts and Talons*); and

(g) in the case of Bearer Bonds, any Global Bond to the extent that it shall have been exchanged for Definitive Bonds or another Global Bond and, in the case of Registered Bonds, any Global Bond Certificate to the extent that it shall have been exchanged for Individual Bond Certificates, and, in each case, pursuant to its provisions, the provisions of the Bond Trust Deed and the Agency Agreement,

PROVIDED THAT for each of the following purposes, namely:

(i) the right to attend and vote at any meeting of the holders of the Bonds of any Sub-Class;

(ii) the determination of how many and which Bonds of any Sub-Class are for the time being outstanding for the purposes of Clause 8 of the Bond Trust Deed, Condition 15 (*Meetings of Bondholders, Modification, Waiver and Substitution*), Clause 9 (*Voting, Instructions and Notification of Outstanding Principal Amount of Qualifying Debt*) of the STID and Paragraphs 2, 5, 6 and 13 of Schedule 4 to the Bond Trust Deed;

(iii) any discretion, power or authority (whether contained in the Bond Trust Deed or vested by operation of law) which the Bond Trustee is required, expressly or impliedly, to exercise in or by reference to the interests of the holders of the Bonds of any Sub-Class; and

(iv) the determination by the Bond Trustee whether any event, circumstance, matter or thing is, in its opinion, materially prejudicial to the interests of the holders of the Bonds of any Sub-Class,

those Bonds of the relevant Sub-Class (if any) which are for

the time being held by or on behalf of the Issuer, the other Obligors, or any Associate of the Issuer or the other Obligors (other than any Associate which is a licensed or regulated financial institution which holds Bonds in the ordinary course of its business), in each case as beneficial owner, shall (unless and until ceasing to be so held) be deemed not to remain outstanding.

"**Outstanding Principal Amount**" means, as at any date that the same falls to be determined:

(a) in respect of Wrapped Debt (unless an FG Event of Default has occurred and is continuing in respect of the Financial Guarantor of such Wrapped Debt), the aggregate of any unpaid amounts owing to a Financial Guarantor under a G&R Deed to reimburse it for any amount paid by it under a Financial Guarantee in respect of unpaid principal on such Wrapped Debt and the principal amount outstanding (or the Equivalent Amount) under such Wrapped Debt (including, in the case of Wrapped Bonds, any premium);

(b) in respect of Wrapped Debt (if an FG Event of Default has occurred and is continuing in respect of the Financial Guarantor of such Wrapped Debt), the principal amount outstanding (or the Equivalent Amount) of such Wrapped Debt (including, in the case of Wrapped Bonds, any premium);

(c) in respect of Unwrapped Debt, the principal amount outstanding (or the Equivalent Amount) of such Unwrapped Debt (including, in the case of Wrapped Debt, any premium);

(d) in respect of any Authorised Credit Facilities that are loans (but do not constitute Wrapped Debt), the principal amount (or the Equivalent Amount) of any drawn amounts that are outstanding under such Authorised Credit Facility;

(e) in respect of each Finance Lease, the Equivalent Amount of either (i) prior to an Acceleration of Liabilities (other than a Permitted Lease Termination) under such Finance Lease and subject to any increase or reduction calculated in accordance with Clause 9.9 (*Notification of Outstanding Principal Amount of Qualifying Debt*) of the STID, the highest termination value which may fall due during the Rental Period encompassing such date,

calculated upon the assumptions set out in the cashflow report provided by the relevant Finance Lessor on the first day of each such Rental Period (or in the most recently generated cashflow report which is current on such date) or (ii) following any Acceleration of Liabilities (other than a Permitted Lease Termination) under such Finance Lease, the actual amount (if any) that would be payable to the relevant Finance Lessor in respect of a termination of the leasing of the Equipment on the date of such Acceleration of Liabilities (other than a Permitted Lease Termination);

(f) in respect of each Hedging Agreement, the Equivalent Amount of the amount (if any) that would be payable to the relevant Hedge Counterparty if an early termination date was designated on such date in respect of the transaction or transactions arising under the Hedging Agreement pursuant to the ISDA Master Agreement governing such transaction or transactions and subject to Schedule 8 (*Hedging Policy and Overriding Provisions Relating to Hedging Agreements*) of the CTA; and

(g) in respect of any other Secured Liabilities, the Equivalent Amount of the outstanding principal amount of such debt on such date in accordance with the relevant Finance Document,

all as most recently certified or notified to the Security Trustee, where applicable, pursuant to Clause 9.9 (*Notification of Outstanding Principal Amount of Qualifying Debt*) of the STID.

"**Out-turn Inflation**" means, in respect of any period for which the relevant indices have been published, the actual inflation rate applicable to such period determined by reference to movements in the Retail Price Index adjusted, as appropriate, in the case of capital additions, for any divergence between the actual movement of national construction costs, as evidenced by the Construction Output Price Index (or such other index as the Director General may Specify for the purposes of Condition B, of the Instrument of Appointment or otherwise)) relative to the Retail Price Index from their base levels as used in the most recent Final Determination or IDOK and their relative movement as projected by the Director General for the purposes of that determination, and, in respect of any period, including future periods, for which the relevant indices have not yet been

	published, by reference to forecast rates consistent with the average monthly movement in such indices over the previous 12 months for which published indices are available.
"**Participating Member State**"	means a member state of the European Community that adopts or has adopted the euro as its lawful currency under the legislation of the European Union for European Monetary Union.
"**Partly Paid Bond**"	means a bond issued in the amount as specified in the relevant Final Terms and in respect of which further instalments will be payable in the amounts and on the dates as specified in the relevant Final Terms.
"**Party**"	means in relation to a Finance Document a party to such Finance Document.
"**Paying Agents**"	means, in relation to all or any Sub-Classes of the Bonds, the several institutions (including, where the context permits, the Principal Paying Agent and/or the Registrar) at their respective specified offices initially appointed as paying agents in relation to such Bonds by the Issuer and the Obligors pursuant to the Agency Agreement and/or, if applicable, any successor paying agents at their respective specified offices in relation to all or any Sub-Classes of the Bonds.
"**Payment Date**"	means each date on which a payment is made or is scheduled to be made by an Obligor in respect of any obligations or liability under any Authorised Credit Facility.
"**Payment Priorities**"	means the order of priority of the Permitted Payments to be made by the Issuer on each Payment Date as set out in Chapter 7 "*Summary of the Financing Agreements*" under "*Cash Management*" as adjusted following the taking of any Enforcement Action and following termination of a Standstill (other than pursuant to a waiver or revocation by the Majority Creditors) in accordance with Paragraph 8.12 of Schedule 12 to the CTA.
"**Pension Companies**"	means SWEPST and SWPT.
"**Periodic Information**"	means: (a) SWS' annual charges scheme with details of tariffs: (b) a summary of SWS' strategic business plan at each Periodic Review; (c) SWS' current Procurement Plan (if any); (d) SWS' annual drinking water quality report;

(e) SWS' annual environmental report;

(f) SWS' annual conservation and access report; and

(g) such other periodic information compiled by SWS for Ofwat.

"**Periodic Review**" means the periodic review of K (as that term is defined in the Instrument of Appointment) as provided for in Condition B of the Instrument of Appointment.

"**Periodic Review Effective Date**" means the date with effect from which the new K (as that term is defined in the Instrument of Appointment) will take effect, following a Periodic Review.

"**Periodic Review Period**" means the period commencing on a Periodic Review Effective Date and ending on the next Date Prior.

"**Permanent Global Bond**" means in relation to any Sub-Class of Bearer Bonds a global bond in the form or substantially in the form set out in Schedule 2, Part B to the Bond Trust Deed with such modifications (if any) as may be agreed between the Issuer, the Principal Paying Agent, the Bond Trustee and the Relevant Dealers, together with the copy of each applicable Final Terms annexed thereto, comprising some or all of the Bearer Bonds of the same Sub-Class, issued by the Issuer pursuant to the Dealership Agreement or any other agreement between the Issuer and the relevant Dealer(s) relating to the Programme, the Agency Agreement and the Bond Trust Deed in exchange for the whole or part of any Temporary Global Bond issued in respect of such Bearer Bonds.

"**Permitted Acquisition**" means any of the following carried out by SWS:

(a) an acquisition (including Authorised Investments), but not of any company or shares therein, partnership or Joint Venture, made on arm's length terms and in the ordinary course of trade;

(b) an acquisition of assets required to replace surplus, obsolete, worn-out, damaged or destroyed assets which in the reasonable opinion of SWS are required for the efficient operation of its Business or in accordance with the Finance Leases;

(c) an acquisition of assets (but not of any company or shares therein, partnership or Joint Venture) made on arm's length terms entered into for bona fide commercial purposes in furtherance of SWS' statutory and regulatory obligations;

(d) an inset business in the United Kingdom which is or will be included in RCV and which breaches neither the Instrument of Appointment nor the WIA; and

(e) any acquisition made or Joint Venture entered into with the consent of the Security Trustee and each Financial Guarantor.

"**Permitted Book Debt Disposal**" means the disposal of book debts in each financial year with a nominal value of up to £5,000,000 (indexed) (or a greater amount with the prior written consent of the Security Trustee and each Financial Guarantor) by SWS on arm's length terms to any person other than an Affiliate, where:

(a) such book debts are sold to a person or persons whose business is the recovery of debts;

(b) SWS has made a prudent provision in its accounts against the non-recoverability of such debts;

(c) any write-back of any provision for non-recoverability arising from the sale can only be treated as operating profit for the purposes of the financial ratios once the relevant recourse period against SWS has expired; and

(d) the SWS Business Financial Model is updated to ensure that the transaction is taken into account in calculating all relevant financial ratios under the CTA.

"**Permitted Disposal**" means any disposal made by SWS which:

(a) is made in the ordinary course of trading of the disposing entity or in connection with an arm's length transaction entered into for bona fide commercial purposes for the benefit of the Business;

(b) is of assets in exchange for other assets comparable or superior as to type, value and quality;

(c) is of Equipment pursuant to the Finance Leases;

(d) would not result in the Senior RAR, calculated for each Test Period by reference to the most recently occurring Calculation Date (adjusted on a pro-forma basis to take into account the proposed disposal), being more than or equal to 0.900:1;

(e) is a disposal for cash on arm's length terms of any surplus or obsolete or worn-out assets which, in the reasonable opinion of SWS, are not required for the efficient operation of its Business and which does not

cause a Trigger Event under Paragraph 1, Part 1 (*Trigger Events*) of Schedule 6 to the CTA;

(f) is made pursuant to the Outsourcing Policy;

(g) is a Permitted Book Debt Disposal;

(h) is a disposal of Protected Land (as that term is defined in the WIA) in accordance with the terms of the Instrument of Appointment;

(i) is a disposal or surrender of tax losses which is a Permitted Tax Loss Transaction;

(j) is the disposal of assets owned by SWS which form part of its Permitted Non-Appointed Business;

(k) is any other disposal which is in accordance with the Instrument of Appointment provided that the consideration (both cash and non-cash) received by SWS (or which would be received by SWS if such disposal was made on arm's length terms for full commercial value to an unconnected third party) in respect of any such disposal when aggregated with all other such disposals by it made in (i) the immediately preceding 12 month period does not exceed 2.5 per cent. of RCV (or its equivalent) and (ii) in the immediately preceding five-year period does not exceed 10 per cent. of RCV (or its equivalent); or

(l) is a disposal of assets to a partnership or a Joint Venture made on arm's lengths terms entered into for bona fide commercial purposes in furtherance of SWS' statutory and regulatory obligations,

provided that in each case such disposal does not cause any of the Trigger Event Ratio Levels to be breached.

"Permitted Emergency Action" means any remedial action taken by SWS during an Emergency which is in accordance with the policies, standards and procedures for emergency planning manual (EMPROC) of SWS (as amended from time to time), Ofwat guidance notes and Public Procurement Rules and which SWS considers necessary and which continues only so Long as required to remedy the Emergency but in any event no longer than 28 days or such longer period as is agreed by SWS, the Security Trustee and each Financial Guarantor.

"Permitted Existing Non-Appointed Business" means any business other than the Appointed Business which is carried on by SWS at the Initial Issue Date and (a) which falls within the Permitted Non-Appointed Business

Limits applicable to Permitted Existing Non-Appointed Business, 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 SWS that are not properly provided for in its financial statements.

"Permitted Existing Pension Schemes" means (i) the SWPS (ii) the SWEPS, (iii) the ScottishPower group Final Salary Scheme, (iv) the ScottishPower group Money Purchase LifePlan, (v) the Manweb Group of the Electricity Supply Pension Scheme and (vi) the Scottish Power group Pension Scheme.

"Permitted Financial Indebtedness" means:

(a) Financial Indebtedness incurred under the Issuer/SWS Loan Agreements;

(b) Financial Indebtedness incurred by one member of the SWS Financing Group to another member if the recipient of that Financial Indebtedness is an Obligor;

(c) Financial Indebtedness incurred under any Finance Document as at the Initial Issue Date;

(d) Financial Indebtedness incurred under a Treasury Transaction provided it is in compliance with the Hedging Policy;

(e) any unsecured indebtedness provided that the aggregate amount of such Financial Indebtedness does not exceed £25,000,000 (indexed);

(f) any Subordinated Debt entered into after the Initial Issue Date and the SWS Preference Shares;

(g) such further Financial Indebtedness incurred by the Issuer or SWS that complies with the following conditions:

(i) at the time of incurrence of that Financial Indebtedness, no Default is continuing or will arise as a result of the incurrence of such Financial Indebtedness;

(ii) the Financial Indebtedness is made available pursuant to an Authorised Credit Facility Agreement the provider of which is a party to, or has acceded to, the CTA and STID;

(iii) as a result of the incurrence of the Financial Indebtedness:

(A) SWS and the Issuer will not be in breach of Paragraph 4 (*DSR Liquidity Facility*) of Part 2 of Schedule 5 (*Financial Covenants*) and Paragraph 38 (*Control of Repayment Schedules*) of Part 3 (*General Covenants*) of Schedule 5 (*Covenants*) to the CTA; and

(B) no Authorised Credit Provider will have substantially better or additional Entrenched Rights under the STID than those Authorised Credit Providers providing similar Financial Indebtedness of the same class; and

(C) the Hedging Policy shall continue to be complied with in all respects;

(iv) the Financial Indebtedness which is Class A Debt ranks (save for, if applicable, any Financial Guarantee) *pari passu* in all respects with all other Class A Debt and the Financial Indebtedness that is Class B Debt ranks (save for, if applicable, any Financial Guarantee) *pari passu* in all respects with all other Class B Debt;

(v) if such further Financial Indebtedness is Class A Debt or Class B Debt then the Senior RAR (adjusted on a pro forma basis to take into account the proposed incurrence of such further Financial Indebtedness) must be less than or equal to 0.900:1 for each Test Period calculated by reference to the then most recently occurring Calculation Date;

(vi) if such further Financial Indebtedness is Class A Debt then (taking into account the proposed incurrence of such debt) the Class A RAR must be less than or equal to 0.75:1 and the Class A Adjusted ICR must be greater than or equal to 1.30:1 for each Test Period calculated by reference to the then most recently occurring Calculation Date; and

(vii) if such further Financial Indebtedness is incurred under a Finance Lease, the amount of that Financial Indebtedness, when aggregated with all other Financial Indebtedness under Finance Leases, shall not exceed an amount 15 per cent. of RCV or its equivalent.

For the purposes of this definition only, the termination

sums payable under a Treasury Transaction that has been terminated shall not be treated as Financial Indebtedness and the occurrence of such event shall not be construed as the incurrence of Financial Indebtedness.

"Permitted Hedge Termination" means the termination of a Hedging Agreement in accordance with the provisions of Schedule 8 (*Hedging Policy and Overriding Provisions Relating to Hedging Agreements*) of the CTA.

"Permitted Lease Termination" means any termination of the leasing of all or any part of the Equipment (or the prepayment of the Rentals arising by reason of such termination) in the following circumstances:

a) Total Loss: Pursuant to any provision of a Finance Lease whereby the leasing of all or any part of the Equipment thereunder will terminate following a total loss of such Equipment save that SWS or the Issuer (as applicable) will not make payment to the relevant Finance Lessor of any sums due and payable under the relevant Finance Lease in respect of such total loss if (I) an Acceleration of Liabilities other than Permitted Hedge Terminations and Permitted Lease Terminations in respect of other Finance Leases has occurred or (ii) a Default Situation is subsisting or would occur as a result of such payment;

(b) Illegality: Pursuant to any provision of a Finance 22

(c) Voluntary Prepayment/Termination: Pursuant to any provision of a Finance Lease whereby SWS or the Issuer (as applicable) will be entitled to voluntarily terminate (and require payment of a termination sum), or prepay the Rentals due to, the leasing of certain Equipment under such Finance Lease provided that (i) no Acceleration of Liabilities other than Permitted Hedge Terminations and Permitted Lease Terminations in respect of other Finance Leases has occurred or (ii) no Default Situation is subsisting or would occur as a result of such prepayment or termination.

"Permitted New Non-Appointed Business" means any business 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 SWS 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 Director General; and (iii) falls within the Permitted Non-

Appointed Business Limits applicable to Permitted Non-Appointed Business; (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 SWS that are not properly provided for in its financial statements.

"Permitted Non-Appointed Business" means Permitted Existing Non-Appointed Business and Permitted New Non-Appointed Business.

"Permitted Non-Appointed Business Income" means income received by SWS pursuant to its Permitted Non-Appointed Business

"Permitted Non-Appointed Business Limits" means, in respect of Permitted Non-Appointed Business, that the average of the Non-Appointed Expenses during the current Test Period and the immediately two preceding Test Periods does not exceed 2.5 per cent. of Cash Expenses of SWS during such Test Periods.

"Permitted Payments" means the application of monies credited to the Debt Service Payment Account in accordance with the Payment Priorities.

"Permitted Post Closing Events" means:

(a) payment of transaction fees and expenses to the extent not paid on the Initial Issue Date: or

(b) payments of all amounts outstanding under the Bridge Facility Agreement and related documentation and the discharge of the security created under such document; or

(c) any other payments listed in writing by SWS as at the Initial Issue Date and signed by way of approval by the Security Trustee.

"Permitted Security Interest" means any security interest falling under paragraphs (a) to (g) (inclusive) below which is created by any Obligor, any security interest falling under paragraphs (h) to (k) (inclusive) below which is created by SWS or the Issuer and any security interest falling under paragraphs (l) to (r) (inclusive) below which is created by SWS:

(a) Security Interest created under the Security Documents or contemplated by the Finance Documents;

(b) any Security Interest specified in Schedule 12 *(Cash Management)* to the CTA, if the principal amount thereby secured is not increased;

(c) a Security Interest comprising a netting or set-off

arrangement entered into by a member of the SWS Financing Group in the ordinary course of its banking arrangements;

(d) a right of set-off, banker's liens or the like arising by operation of law or by contract by virtue of the provision of any overdraft facility and like arrangements arising as a consequence of entering into arrangements on the standard terms of any bank providing an overdraft;

(e) any Security Interest arising under statute or by operation of law in favour of any government, state or local authority in respect of taxes, assessments or government charges which are being contested by the relevant member of the SWS Financing Group in good faith and with a reasonable prospect of success;

(f) any Security Interest created in respect of any pre-judgment legal process or any judgment or judicial award relating to security for costs, where the relevant proceedings are being contested in good faith by the relevant member of the SWS Financing Group by appropriate procedures and with a reasonable prospect of success;

(g) a security interest comprising a netting or set-off arrangement entered into under any hedge arrangement entered into in accordance with the Hedging Policy where the obligations of other parties thereunder are calculated by reference to net exposure thereunder (but not any netting or set-off relating to such hedge arrangement in respect of cash collateral or any other Security Interest except as otherwise permitted hereunder);

(h) a lien in favour of any bank over goods and documents of title to goods arising in the ordinary course of documentary credit transactions entered into in the ordinary course of trade

(i) a Security Interest created over shares and/or other securities acquired in accordance with the CTA held in any clearing system or listed on any exchange which arise as a result of such shares and/or securities being so held in such clearing system or listed on such exchange as a result of the rules and regulations of such clearing system or exchange;

(j) a Security Interest approved by the Security Trustee,

the holder of which has become a party to the STID;

(k) a Security Interest over or affecting any asset acquired on arm's length terms after the date hereof and subject to which such asset is acquired, if:

(i) such Security Interest was not created in contemplation of the acquisition of such asset;

(ii) the amount thereby secured has not been increased in contemplation of, or since the date of, the acquisition of such asset by a member of the SWS Financing Group; and

(iii) unless such Security Interest falls within any of paragraphs (m) to (r) below (A) such Security Interest is removed or discharged within six months of the date of acquisition of such asset; or (B) the holder thereof becomes party to the STID;

(l) a Security Interest arising in the ordinary course of business and securing amounts not more than 90 days overdue or if more than 90 days overdue, the original deferral was not intended to exceed 90 days and such amounts are being contested in good faith;

(m) a Security Interest arising under or contemplated by any Finance Leases, hire purchase agreements, conditional sale agreements or other agreements for the acquisition of assets on deferred purchase terms where the counterparty becomes party to the STID;

(n) a right of set-off existing in the ordinary course of trading activities between SWS and its suppliers or customers;

(o) a lien arising under statute or by operation of law (or by agreement having substantially the same effect) and in the ordinary course of business provided that such lien is discharged within 30 days of any member of the SWS Financing Group becoming aware that the amount owing in respect of such lien has become due;

(p) a Security Interest arising on rental deposits in connection with the occupation of leasehold premises in the ordinary course of business; or

(q) any retention of title arrangements entered into by SWS in the ordinary course of business; or

(r) in addition to any Security Interests subsisting pursuant to the above any other Security Interests provided that the aggregate principal amount secured by such Security Interests does not at any time exceed £10,000,000 (or its equivalent) (indexed),

to the extent and for so long, in each case, as the creation or existence of the Security Interest would not contravene the terms of the Instrument of Appointment, the WIA or any requirement under the Instrument of Appointment or the WIA.

"Permitted Share Pledge Acceleration" means the acceleration by the Secured Creditors (subject to the availability of funds) of their respective claims to the extent necessary to apply proceeds of enforcement of the share pledges provided by SWSGH and SWSH pursuant to the Security Agreement.

"Permitted Subsidiaries" means the Pension Companies and the Issuer and any other Subsidiary of SWS from time to time which is acquired by SWS pursuant to a Permitted Acquisition and is notified in writing to the Security Trustee on or as soon as practicable after the date of such acquisition.

"Permitted Tax Loss Transaction" means any surrender of tax losses or agreement relating to tax benefit or relief (including for the avoidance of doubt an election under section 171A Taxation of Chargeable Gains Act 1992) or any other agreement relating to tax between:

(a) an Obligor and any other member of the SWS Financing Group; or

(b) an Obligor and any other member of the Group (not being a member of the SWS Financing Group) in the following circumstances

(i) where the company receiving the benefit, tax loss or relief (the "**Recipient Company**") is an Obligor, the Obligor either makes no payment for the benefit, tax loss or relief or makes a payment which does not exceed the tax saved and is made only in circumstances in which (if SWS is the Recipient Company and SWSG is the surrendering company) it will be applied in immediate payment to SWS of interest due and payable under the SWS/SWSG Loan Agreement or in which it has been demonstrated to the satisfaction of the Security Trustee (acting in accordance with STID) that the utilisation of the benefit, tax loss or relief by the Recipient Company would not be subject to challenge by HM Revenue

and Customs (save in the event of fraud or negligence);

(ii) where the Recipient Company is a member of the Group (other than an Obligor), a payment is made to the Obligor of an amount equal to the tax saved within 30 days of the claim being made by the Recipient Company to include the benefit, tax loss or relief in the tax return (whether the tax return originally filed or an amendment to that tax return) it files with HM Revenue and Customs, provided that to the extent that it is subsequently demonstrated to the satisfaction of the Security Trustee (acting in accordance with the STID) that there is no such utilisation of such benefit, tax loss or relief by the Recipient Company, then amounts paid to the Obligor by the Recipient Company for such benefit, tax loss or relief should be refunded within 30 days of such fact being so demonstrated.

"Permitted Volume Trading Arrangements" means contracts entered into by any member of the Group or any Associate thereof with suppliers for the supply of goods and services to the SWS Financing Group on terms that discounts are available as a result of such arrangements, provided that any Obligor making use of such arrangements will reimburse the relevant member of the Group or Associate for any Financial Indebtedness by way of amounts payable by such member of the Group or Associate to such supplier as a result of such Obligor making use of such arrangements.

"Potential Event of Default" means (other than in any Hedging Agreement, where **"Potential Event of Default"** has the meaning given to it in that Hedging Agreement) an event which would be (with the expiry of a grace period, the giving of notice or the making of any determination under the Finance Documents or any combination of them) an Event of Default.

"Potential Trigger Event" means any event which would (with the expiry of any relevant grace period or the giving of notice or any combination thereof) if not remedied or waived become a Trigger Event.

"Principal Amount Outstanding" means, in relation to a Bond, Sub-Class or Class, the original face value thereof less any repayment of principal made to the holder(s) thereof in respect of such Bond, Sub-Class or Class.

"Principal Paying Agent" means Deutsche Bank AG London under the Agency Agreement, or its Successors thereto.

"Proceeds"	means the aggregate of all receipts or recoveries by the Security Trustee pursuant to, or upon enforcement of, any of the Rights (including pursuant to Clause 11.6 *(Receipts Held in Trust)* of the STID) after deducting (to the extent not already deducted or retained prior to such receipt or recovery by the Security Trustee) all sums which the Security Trustee is required under the Finance Documents or by applicable law to pay to any other person before distributing any such receipts or recoveries to any of the Secured Creditors.
"Procurement Plan"	means the procurement plan (if any) prepared and amended from time to time by SWS in accordance with its obligations under the Instrument of Appointment after notifying the Security Trustee and each Financial Guarantor and consulting with the Security Trustee and each Financial Guarantor who, within reasonable time thereafter, notifies SWS that it wishes to be consulted.
"Programme"	means the £6,000,000,000 guaranteed bond programme established by the Issuer admitted to the Official List and to the London Stock Exchange.
"Projected Operating Expenditure"	means at any time, the operating expenditure projected in the operating budget for the Test Period in which such date falls.
"Prospectus"	has the meaning given to that term on page 7 of this prospectus.
"Protected Land"	means, in relation to a Regulated Company any land which, or any interest or right in or over land which: (a) was transferred to that company in accordance with a scheme under Schedule 2 to the Water Act 1989 or, where that company is a statutory water company (as defined in the WIA), was held by that company at any time during the financial year ending 31 March 1990; (b) is or has at any time on or after 1 September 1989 been held by that company for purposes connected with the carrying out of its functions as a water undertaker or sewerage undertaker; or (c) has been transferred to that company in accordance with a scheme under Schedule 2 to the WIA from another company in relation to which that land was protected when the other company held an instrument of appointment.
"**PSM**"	means the London Stock Exchange's Professional Securities Market.

"Public Procurement Rules"	means public procurement rules of the United Kingdom (including the Utilities Contracts Regulations 1996 (SI 1996/2911) as amended by the Utilities Contracts (Amendment) Regulations 2001 (SI 2001/2418)) and of the European Communities (including Directive 93/98 as amended by Directive 98/4) affecting the water and sewerage sector and including any jurisprudence of the courts of the United Kingdom and of the European Communities and decisions of the European Commission in respect of such rules
"Qualifying Class A Debt"	means the aggregate Outstanding Principal Amount of Class A Debt entitled to be voted by the Class A DIG Representatives.
"Qualifying Class A Debt Provider"	means a provider of Qualifying Class A Debt.
"Qualifying Class B Debt"	means the aggregate Outstanding Principal Amount of Class B Debt entitled to be voted by the Class B DIG Representatives.
"Qualifying Class B Debt Provider"	means a provider of Qualifying Class B Debt.
"Qualifying Debt"	means the Qualifying Class A Debt, the Qualifying Class B Debt, the Senior Mezzanine Debt or Junior Mezzanine Debt, as the context requires.
"Rating Agencies"	means Fitch, Moody's and S&P and any further or replacement rating agency appointed by the Issuer with the approval of the Security Trustee (acting upon the instructions of the Majority Creditors) to provide a credit rating or ratings for the Class A Debt and the Class B Debt and shadow ratings in respect of Class A Wrapped Debt and Class B Wrapped Debt for so long as they are willing and able to provide credit ratings generally (and **"Rating Agency"** means any one of them).
"Rating Requirement"	means confirmation from any two Rating Agencies or, where expressly stated, all Rating Agencies then rating the Bonds that, in respect of any matter where such confirmation is required, the shadow rating is, in the case of the Class A Wrapped Debt, A- by Fitch and S&P and A3 by Moody's or above and in the case of the Class A Unwrapped Debt, is A- by Fitch and S&P and A3 by Moody's or above.
"RBS"	means The Royal Bank of Scotland plc.
"RBSG"	means The Royal Bank of Scotland Group plc, a company incorporated in Scotland and ultimate holding company of

the RBS Group.

"RBS Group" means RBSG and its Subsidiaries.

"RCV" means, in relation to any date, the regulatory capital value for such date as last determined (excluding any draft determination of the regulatory capital value by the Director General) and notified to SWS by the Director General at the most recent Periodic Review or IDOK or other procedure through which in future the Director General may make such determination on an equally definitive basis to that of a Periodic Review or IDOK (interpolated as necessary and adjusted as appropriate for Out-turn Inflation), provided that **"RCV"** for the purposes of calculating the Senior RAR and Class A RAR for any Test Period for which there is no Final Determination shall be SWS' good faith, honestly held present estimate of its regulatory capital value on the last day of such Test Period.

"Receipt" means a receipt attached on issue to a Definitive Bond redeemable in instalments for the payment of an instalment of principal and includes any replacements for Receipts and Talons issued pursuant to Condition 14 *(Replacement of Bonds, Coupons, Receipts and Talons).*

"Receiptholders" means the several persons who are for the time being holders of the Receipts.

"Register" Means a register of the Bondholders of a Sub-Class of Registered Bonds.

"Registered Bonds" means those of the Bonds which are for the time being in registered form.

"Registered Office Agreement" means the registered office agreement dated 1 January 2002 between the Issuer, Maples and Calder and M&C Corporate Services Limited.

"Registrar" means Deutsche Bank Luxembourg S.A. as a registrar under the Agency Agreement and any other entity appointed as a registrar under the Agency Agreement.

"Regulated Company" means a company appointed as a water undertaker or a water and sewerage undertaker under section 6 of the WIA.

"Regulation S" has the meaning given to such term under the Securities Act.

"Relevant Authorisation" means all consents, licences, authorisations and approvals (including any such as may be required pursuant to the Instrument of Appointment):

(a) necessary to enable the consummation of the transactions constituted by the Finance Documents to

which SWS is a party;

(b) (including the Instrument of Appointment) necessary for the conduct of the business of SWS substantially as conducted at the date hereof and for the leasing of the Equipment; and

(c) any other consent, licence or authorisation required in accordance with the normal course of business or good industry practice,

and in each case, which if not obtained or complied with or which if revoked or terminated would have a Material Adverse Effect.

"Relevant Date" has the meaning set out in Condition 6(i) *(Definitions).*

"Remedial Plan" means any remedial plan agreed by SWS and the Security Trustee under Part 2 of Schedule 6 *(Trigger Events)* of the CTA.

"Rental" means any scheduled payment of rental, periodic charge or equivalent sum under a Finance Lease.

"Rental Payment Date" means any date on which Rental is scheduled to be paid under any Finance Lease.

"Rental Period" means, in respect of a Finance Lease, each period falling between two Rental Payment Dates under the Finance Lease.

"Repeated Representations" means:

(a) the representations set out in Paragraphs 1 to 3, 8 to 10, 12 to 14 and 17 to 19 (inclusive) of Schedule 3 *(General Representations)* of the CTA;

(b) the representations set out in Paragraphs 1 and 5 of Schedule 4 *(SWS representations)* of the CTA;

And which are deemed, pursuant to the CTA to be repeated on:

- the date of each Request and the first day of any borrowing;
- each Payment Date;
- in relation to any new Material Agreement, the day on which such agreement is entered into and only in relation to such new Material Agreement; and
- each date on which a Restricted Payment is made.

See Chapter 7 *"Summary of the Financing Agreements" under "Common Terms Agreement — Representations"*.

"Request"	means a request for utilisation of any Authorised Credit Facility.
"Required Balance"	means the sum of the Class A Required Balance and the Class B Required Balance.
"Reserved Matters"	means matters which, subject to the Intercreditor Arrangements, a Secured Creditor is free to exercise in accordance with its own facility arrangements and not by the direction of the Majority Creditors as more particularly described in the STID.
"Restricted Chargors"	means each of the Issuer and SWS and any other entity which accedes to the Security Agreement pursuant to Clause 27.3 *(Assignments and transfers)* thereof that is restricted from providing guarantees by its regulatory or statutory obligations.
"Restricted Payment"	means any Distribution, Customer Rebate, or payment under the Subordinated Debt or the SWS Preference Shares other than: (a) to the extent required to make any payment under an Authorised Credit Facility in accordance with the provisions of the CTA and the STID, a payment by SWS under any Issuer/SWS Loan Agreement; or (b) a payment made under a Permitted Tax Loss Transaction; or (c) any Permitted Post-Closing Event; (d) a Subordinated Debt Replacement Event or SWS Preference Share Conversion Event; or (e) an SWS/SWSG Debt Service Distribution.
"Restricted Payment Condition"	means each of the conditions which must be satisfied or waived by the Security Trustee before a Restricted Payment may be made by the Issuer or SWS.
"Restricted Secured Liabilities"	means all present and future obligations and liabilities (whether actual or contingent and whether owed jointly or severally or in any other capacity whatsoever) of each Restricted Chargor to any Secured Creditor under each Finance Document to which such Restricted Chargor is a party, except for any obligation which, if it were secured under the Security Agreement, would result in a contravention of Section 151 of the Companies Act 1985.
"Retail Price Index" or **"RPI"**	means the all items retail prices index for the United Kingdom Published by the Office for National Statistics or at any future date such other index of retail prices as may

have then replaced it for the purposes of the Director General's determination of price limits for water and sewerage services.

"Rights"	means all rights vested in the Security Trustee by virtue of, or pursuant to, its holding the interests conferred on it by the Security Documents or under the Ancillary Documents and all rights to make demands, bring proceedings or take any other action in respect of such rights.
"Rolling Average Period"	means on each Calculation Date the Test Period ending on 31 March that falls in the same calendar year as that Calculation Date and the next subsequent two consecutive Test Periods.
"S&P"	means Standard & Poor's Ratings Services, a Division of the McGraw Hill Companies Inc., or any successor to the rating agency business of S&P.
"Scheduled Debt Service"	means the amounts referred to in sub-paragraphs (i)-(xii) of the Payment Priorities (other than principal repayments on the Class A Debt and Class B Debt) payable on a particular Payment Date.
"Second Artesian Term Facility"	means the £155,484,023.05 index-linked term facility made available to the Issuer by Artesian.
"Second Artesian Term Facility Agreement"	means a facility agreement dated 5 July 2004 under which the Second Artesian Term Facility was made available to the Issuer and includes that facility agreement in the form amended and restated at the time of the novation of such facility agreement to Artesian.
"Second Issue Date"	means 5 July 2004.
"Second Issuer/SWS Loan Agreement"	means the loan agreement entered into between the Issuer and SWS on 5 July 2004.
"Second RCF Providers"	means the Finance Parties party to the Second Revolving Credit Facility.
"Second Revolving Credit Facility"	means the revolving credit facility of an aggregate facility amount of £120,000,000 made available to SWS by RBS and Bayerische Landesbank, London Branch on 30 June 2005.
"Secretary of State"	means one of Her Majesty's principal secretaries of state;
"Secured Creditor"	means the Security Trustee (in its own capacity and on behalf of the other Secured Creditors), the Bond Trustee (in its own capacity and on behalf of the Bondholders), the Bondholders, each Financial Guarantor, the Hedge Counterparties, the Issuer, the Liquidity Facility Agents,

each Liquidity Facility Provider, the Initial Authorised Credit Facility Arranger, the Initial Authorised Credit Facility Agent, the Initial Authorised Credit Provider, Artesian II, Artesian and each other Authorised Credit Provider, the Standstill Cash Manager, each Agent, the Mezzanine Finance Parties, and any Additional Secured Creditors.

"Secured Creditor Representative" means:

(a) in respect of the Bondholders, the Bond Trustee

(b) in respect of the Initial RCF Providers, the Initial RCF Agent;

(c) in respect of Artesian II, Artesian II;

(d) in respect of Artesian, Artesian;

(e) in respect of the Issuer/SWS Loan Agreements, the Security Trustee (on behalf of the Issuer);

(f) in respect of any Liquidity Facility Provider, the facility agent under the relevant Liquidity Facility Agreement;

(g) in respect of the Senior Mezzanine Finance Parties, the Senior Mezzanine Facility Agent;

(h) in respect of the Junior Mezzanine Finance Parties, the Junior Mezzanine Facility Agent; and

(i) in respect of any Additional Secured Creditor, the representative of such Additional Secured Creditor (if any) appointed as its Secured Creditor Representative under the terms of the relevant Finance Document and named as such in the relevant Accession Memorandum.

"Secured Liabilities" means the Restricted Secured Liabilities and the Unrestricted Secured Liabilities.

"Securities Act" means the United States Securities Act of 1933, as amended.

"Security" means the security constituted by the Security Documents including any Guarantee or obligation to provide cash collateral or further assurance thereunder.

"Security Agreement" means the deed of charge and guarantee executed in favour of the Security Trustee by each of the Obligors on the Initial Issue Date.

"Security Assets" means all property, assets, rights and undertakings the subject of the Security created by the Obligors pursuant to

any Security Document, together with the Rights.

"Security Documents" means:

(a) the Security Agreement;

(b) the STID and each deed of accession thereto; and

(c) any other document evidencing or creating security over any asset of an Obligor to secure any obligation of any Obligor to a Secured Creditor under the Finance Documents.

"Security Interest" means:

(a) any mortgage, pledge, lien, charge, assignment, or hypothecation, or other encumbrance securing any obligation of any person;

(b) any arrangement under which money or claims to money, or the benefit of, a bank or other account may be applied, set off or made subject to a combination of accounts so as to effect discharge of any sum owed or payable to any person; or

(c) any other type of preferential arrangement (including any title transfer and retention arrangement) having a similar effect.

"Security Trustee" means Deutsche Trustee Company Limited or any successor appointed pursuant to the STID.

"Senior Adjusted ICR" means, in respect of a Test Period, the ratio of Net Cash Flow less the aggregate of CCD and IRC during such Test Period to Senior Debt Interest during such Test Period.

"Senior Average Adjusted ICR" means the sum of the ratios of Net Cash Flow less the aggregate of CCD and IRC to Senior Debt Interest for each of the Test Periods comprised in a Rolling Average Period divided by three.

"Senior Debt" means all Class A Debt and Class B Debt and any other debt ranking in priority to subordinated debt of any member of the SWS Financing Group.

"Senior Debt Interest" means, in relation to any Test Period and without double counting, an amount equal to the aggregate of:

(a) all interest paid, due but unpaid or, in respect of forward-looking ratios, payable, on the Issuer's and/or SWS' obligations under and in connection with all Class A Debt and Class B Debt;

(b) all interest paid, due but unpaid or, in respect of forward-looking ratios, payable under or in

connection with any Permitted Financial Indebtedness falling within paragraph (e) of that definition;

(c) all fees paid, due but unpaid or, in respect of forward-looking ratios, payable, to any Financial Guarantor; and

(d) Adjusted Lease Reserve Amounts or Lease Reserve Amounts paid, due but unpaid or, in respect of forward-looking ratios, payable, on the Issuer's and/or SWS' obligations under and in connection with all Class A Debt and Class B Debt,

in each case during such Test Period (after taking account of the impact on interest rates of all related Hedging Agreements then in force) (excluding all indexation of principal to the extent it has been included in such interest or other amounts, amortisation of the costs of issue of any Class A Debt and Class B Debt within such Test Period and all other costs incurred in connection with the raising of such Class A Debt or Class B Debt) less all interest received or, in respect of forward-looking ratios, receivable by any member of the SWS Financing Group from a third party during such Test Period (excluding any interest received or receivable from SWSG under the SWS/SWSG Loan Agreement).

"Senior Mezzanine Debt" means the principal amount outstanding for the time being under the loan made by the Senior Mezzanine Facility Providers under the Senior Mezzanine Facility Agreement.

"Senior Mezzanine Facility" means a credit facility in the amount of £127,200,000 provided by the Senior Mezzanine Facility Providers to the Issuer pursuant to the Senior Mezzanine Facility Agreement.

"Senior Mezzanine Facility Agent" means The Royal Bank of Scotland plc or any successor thereto as agent under the Senior Mezzanine Facility Agreement.

"Senior Mezzanine Facility Agreement" means the £127,200,000 senior mezzanine facility agreement dated the Initial Issue Date between the Issuer, the Senior Mezzanine Facility Agent, the Senior Mezzanine Facility Arranger, the Original Senior Mezzanine Facility Provider and the Security Trustee.

"Senior Mezzanine Facility Arranger" means RBEF Limited.

"Senior Mezzanine Facility Providers" means the "Lenders" (as defined in the Senior Mezzanine Facility Agreement).

"Senior Mezzanine Finance Parties" means:

(a) the Senior Mezzanine Facility Agent;

(b) the Senior Mezzanine Facility Arranger; and

(c) the Senior Mezzanine Facility Providers.

"Senior Net Indebtedness" means, as at any date, all the Issuer's and SWS' nominal debt outstanding (or, in respect of a future date, forecast to be outstanding) under and in connection with any Class A Debt and Class B Debt on such date and the nominal amount of any Financial Indebtedness falling within paragraph (e) of the definition of Permitted Financial Indebtedness which is outstanding (or, in respect of a future date, forecast to be outstanding) on such date including, in each case, all indexation accrued but unpaid up to and including such date (after taking account of the impact on interest rates of all related Hedging Agreements then in force) on any such liabilities which are indexed together with any interest due and unpaid (after taking account of the impact on interest rates of all related Hedging Agreements then in force) and less the value of all Authorised Investments and all other amounts standing to the credit of any Account (other than an amount equal to the Excluded Insurance Proceeds Amount an amount equal to the aggregate of any amounts which represent Customer Rebates or Distributions which have been declared but not paid on such date) (where such debt is denominated other than in pounds sterling, the nominal amount outstanding will be calculated (i) in respect of debt with associated Currency Hedging Agreements, by reference to applicable hedge rates; or (ii) in respect of debt with no associated Currency Hedging Agreements, by reference to the Exchange Rate on such date).

"Senior RAR" means, on any Calculation Date, the ratio of Senior Net Indebtedness to RCV as at such Calculation Date or, in the case of forward-looking ratios in respect of Test Periods ending after such Calculation Date, as at the 31 March falling in such Test Period.

"Series" means a series of Bonds issued under the Programme on a

particular Issue Date, together with any Tranche or Tranches of Bonds which are expressed to be consolidated and form a single Sub-Class with any Sub-Class issued on such Issue Date.

"Series 1 Bonds"	means the Issuer's Series 1 Bonds issued on the Initial Issue Date, as further defined in Chapter 3 *(Summary Financing Structure)*.
"Series 1 Redeemed Bonds"	has the meaning given to that term on page 26 of this Prospectus.
"Series 2 Bonds"	means the Issuer's Series 2 Bonds issued on the Third Issue Date, as further defined in Chapter 3 (*Summary Financing Structure*).
"Shareholder Tax Deed of Covenant"	means the deed of covenant entered into on the Initial Issue Date by, among others, the Security Trustee, RBSG and MBIA Assurance S.A.
"Share Pledges"	means the pledges dated on or about the Initial Issue Date, in favour of the Security Trustee, over the shares in SWSH, SWS and the Issuer respectively and **"Share Pledge"** means any one of them.
"Shipwreck Clause"	means a clause which may be contained in the licence of a Regulated Company and which is contained in the Licence of SWS at Part IV of Condition B, pursuant to which the Regulated Company may, if so permitted by the conditions of its licence, request price limits to be reset if the Appointed Business either (i) suffers a substantial adverse effect which could not have been avoided by prudent management action or (ii) enjoys a substantial favourable effect which is fortuitous and not attributable to prudent management action.
"Shortfall Paragraph"	means to the extent that (after payment of all relevant operating expenditure) there is a shortfall of forecast revenues, the relevant sub-paragraph of the Payment Priorities in relation to which the revenue that is forecast to be available is insufficient to meet all of the payments in such sub-paragraph.
"Special Administration"	means the insolvency process specific to Regulated Companies under Sections 23 to 26 of the WIA.
"Special Administration Order"	means an order of the High Court under sections 23 to 25 of the WIA under the insolvency process specific to Regulated Companies.
"Special Administration Petition Period"	means the period beginning with the presentation of the petition for Special Administration under Section 24 of the WIA and ending with the making of a Special Administration Order or the dismissal of the petition.
"Special Administrator"	means the person appointed by the High Court under Sections 23 to 25 of the WIA to manage the affairs, business

and property of the Regulated Company during the period in which the Special Administration Order is in force.

"Standard & Poor's" or **"S&P"**	means Standard & Poor's Ratings Services, a division of the McGraw-Hill Companies Inc. or any successor to the rating business of Standard & Poor's Rating Services.
"Standby Drawing"	means a drawing made under a Liquidity Facility Agreement as a result of a downgrade of a Liquidity Facility Provider below the Required Ratings or in the event that the Liquidity Facility Provider fails to renew its commitment on the expiry of the term of such Liquidity Facility Agreement.
"Standstill"	means, as provided for in Clause 13.1 *(Commencement of Standstill)* of the STID, a standstill of claims of the Secured Creditors against SWS and the Issuer immediately upon notification to the Security Trustee of the occurrence of an Event of Default. See Chapter 7 *(Summary o*f *Financing Agreements)* under *"Security Trust* and *Intercreditor Deed - Standstill"* for a summary.
"Standstill Cash Manager"	means The Royal Bank of Scotland plc in its capacity as Standstill Cash Manager under the CTA, or any successor Standstill Cash Manager.
"Standstill Event"	means an event giving rise to a Standstill in accordance with the STID. See Chapter 7 *(Summary of Financing Agreements)* under *"Security Trust and Intercreditor Deed - Standstill"* for a summary.
"Standstill Extension"	means any of the periods for which a Standstill Period is extended under Clause 13.5 (*Extension of Standstill)* of the STID, See Chapter 7 *(Summary of Financing Agreements)* under *"Security Trust and Intercreditor Deed – Standstil*l *Extension"* for a summary.
"Standstill Period"	means a period during which a standstill arrangement is subsisting, commencing on the date as determined by Clause 13.1 *(Commencement of Standstill)* of the STID and ending on the date as determined by Clause 13.4 *(Termination of Standstill)* of the STID. See Chapter 7 *(Summary of Financing Agreements)* under *"Security Trust and Intercreditor Deed - Standstill"* for a summary.
"Statutory Accounts"	means the statutory accounts which SWS is required to prepare in compliance with the Companies Act 1985, as amended from time to time.
"STID"	means the security trust and intercreditor deed entered into on the Initial Issue Date between, among others, the Security Trustee, the Obligors, the Bond Trustee and the Initial Financial Guarantor, together with any deed supplemental to

the STID and referred to in the STID as a "Supplemental Deed".

"STID Directions Request" means a written notice of each STID Proposal sent by the Security Trustee to the Secured Creditors or their Secured Creditor Representatives and requesting directions from the relevant Secured Creditors in accordance with the STID.

"STID Proposal" means a proposal or request made by any Secured Creditor or its Secured Creditor Representative or any Obligor in accordance with the STID proposing or requesting the Security Trustee: to execute a supplemental deed to the STID; to change, modify or waive any term or condition of any Finance Document; to substitute the Issuer; or to take any Enforcement Action or any other action in respect of the transactions contemplated by the Finance Documents; as defined more particularly in the STID.

"Stock Exchange" means the London Stock Exchange or any other or further stock exchange(s) on which any Bonds may from time to time be listed, and references in these presents (as defined in this Prospectus) to the **"relevant Stock Exchange"** shall, in relation to any Bonds, be references to the Stock Exchange on which such Bonds are, from time to time, or are intended to be, listed.

"Sub-Class" is a division of a Class.

"Subordinated Authorised Loan Amounts" means, in relation to any Authorised Credit Facility, the aggregate of any amounts payable by the Issuer or SWS to the relevant Authorised Credit Provider on an accelerated basis as a result of illegality (excluding accrued interest, principal and recurring fees and commissions) on the part of the Authorised Credit Provider or any other amounts not referred to in any other paragraph of the Payment Priorities.

"Subordinated Coupon Amounts" means, in the case of Fixed Rate Bonds or Indexed Bonds, any amounts (other than deferred interest) by which the Coupon on such Bonds exceeds the initial Coupon as at the date on which such Bonds were issued and, in the case of Floating Rate Bonds, any amounts (other than deferred interest) by which the margin on the Coupon on such Bonds exceeds the initial margin on the Coupon on such Bonds as at the date on which such Bonds were issued.

"Subordinated Debt" means any Financial Indebtedness (other than Financial Indebtedness falling within paragraph (e) of the definition of Permitted Financial Indebtedness) that is fully subordinated, in a manner satisfactory to the Security Trustee and each Financial Guarantor, to the Class A Debt and Class B Debt

and where the relevant credit provider has acceded to the Common Terms Agreement and the STID or upon an SWS Preference Share Conversion Event, the SWS Preference Share Deed, including, for the avoidance of doubt, the Mezzanine Debt.

"Subordinated Debt Replacement Event" means any refinancing of any or all of the Senior Mezzanine Debt or Junior Mezzanine Debt at any time so long as (i) no Event of Default is continuing or would result from such refinancing; (ii) no Trigger Event described in Chapter 7 *"Summary of Financing Agreements" under "Common Terms Agreement: Trigger Events – Financial Ratios"; "Common Terms Agreement: Trigger Events – Liquidity for Capital Expenditure and Working Capital"; "Common Terms Agreement: Trigger Events – Debt Service Required Payment Shortfall*" and *"Common Terms Agreement: Trigger Events – Drawdown on DSR Liquidity Facilities and O&M Reserve Facility"* is continuing; and (iii) the Financial Indebtedness incurred in order to raise funds for such refinancing (which may, for the avoidance of doubt, be by way of subordinated bonds) ranks below the Class B Debt and is on substantially the same terms as the Senior Mezzanine Debt or the Junior Mezzanine Debt, as the case may be, being refinanced.

"Subordinated Liquidity Facility Amounts" means, in relation to any Liquidity Facility:

(a) the amount by which the amount of interest accruing at the Mandatory Cost Rate at any time exceeds the Mandatory Cost Rate on the date of the relevant Liquidity Facility Agreement; and

(b) the aggregate of any amounts payable by the Issuer to the relevant Liquidity Facility Provider in respect of its obligation to gross-up any payments made by it in respect of such Liquidity Facility as a result of such Liquidity Facility Provider ceasing to be a Liquidity Facility Provider or to make any payment of increased costs to such Liquidity Facility Provider (other than any such increased costs in respect of regulatory changes relating to capital adequacy requirements applicable to such Liquidity Facility Provider) or to amounts payable on an accelerated basis as a result of illegality (excluding accrued interest, principal and commitment fees) on the part of such Liquidity Facility Provider, or any other amounts not referred to in any other paragraph of the Payment Priorities.

Subscription Agreement”	means an agreement supplemental to the Dealership Agreement (by whatever name called) substantially in the form set out in Schedule 6 to the Dealership Agreement or in such other form as may be agreed between, among others, the Issuer and the Lead Manager or one or more Dealers (as the case may be).
“Subsidiary”	means: (a) a subsidiary within the meaning of section 736 of the Companies Act 1985; and (b) unless the context otherwise requires, a subsidiary undertaking within the meaning of section 258 of the Companies Act 1985.
“Successor”	means, in relation to the Principal Paying Agent, the other Paying Agents, the Registrar, the Transfer Agent, the Agent Bank and the Calculation Agent, any successor to any one or more of them in relation to the Bonds which shall become such pursuant to the provisions of the Bond Trust Deed and/or the Agency Agreement (as the case may be) and/or such other or further principal paying agent, paying agents, registrar, transfer agents, agent bank and calculation agent (as the case may be) in relation to the Bonds as may (with the prior approval of, and on terms previously approved by, the Bond Trustee in writing) from time to time be appointed as such, and/or, if applicable, such other or further specified offices (in the case of the Principal Paying Agent being within the same city as the office(s) for which it is substituted) as may from time to time be nominated, in each case by the Issuer and the Obligors, and (except in the case of the initial appointments and specified offices made under and specified in the Conditions and/or the Agency Agreement, as the case may be) notice of whose appointment or, as the case may be, nomination has been given to the Bondholders.
“Super-Majority Creditor”	means the Class A DIG Representatives in respect of more than 66⅔ per cent. of the Voted Qualifying Class A Debt or, following the repayment in full of the Class A Debt, the Class B DIG Representatives in respect of more than 66⅔ per cent. of the Voted Qualifying Class B Debt, in each case subject to Clause 8 *(Modifications, Consents and Waivers)* and Clause 9 *(Voting, Instructions and Notification of Outstanding Principal Amounts of Qualifying Debt)* of the STID as summarised in Chapter 7 *“Summary of the Financing Agreements”* under *“Security Trust and Intercreditor Deed – Super-Majority Creditor Decisions”*.

"Supplemental Deed" means a deed supplemental to the STID entered into by the Security Trustee on its own behalf and on behalf of the Secured Creditors in the circumstances referred to in Clause 2.1 *(Accession of Additional Secured Creditor)* or Clause 3 *(Additional Finance Documents)* of the STID.

"Surveillance Letter" means a letter issued by the Issuer and/or SWS to a Financial Guarantor from time to time, in which the Issuer and/or SWS undertakes to provide the relevant Financial Guarantor with certain information and to comply with certain reporting requirements as outlined in that letter.

"**SWC**" means Southern Water Capital Limited.

"**SWC Acquisition**" has the meaning given to that term on page 25 of this Prospectus.

"**SWEPST**" means Southern Water Executive Pension Scheme Trustees Limited.

"**SWI**" means Southern Water Investments Limited.

"**SWPS**" means the Southern Water Pension Scheme for SWS employees.

"**SWPT**" means Southern Water Pension Trustees Limited.

"**SWS**" means Southern Water Services Limited.

"**SWS Business Financial Model**" means the business Financial model prepared by SWS and delivered to the Security Trustee from time to time.

"**SWS Change of Control**" means the occurrence of any of the following events or circumstances:

(a) SWSGH ceasing to hold legally and beneficially all rights in 100 per cent. of the issued share capital of, or otherwise ceasing to control, SWSH;

(b) SWSH ceasing to hold legally and beneficially all rights in 100 per cent. of the issued ordinary share capital of, or otherwise ceasing to control, SWS; or

(c) SWS ceasing to hold legally and beneficially all rights in 100 per cent. of the issued share capital of, or otherwise ceasing to control, the Issuer and the SWS Pension Companies.

"SWS Event of Default" means the events of default set out in Part 2 (*Events of Default (SWS))* of Schedule 7 *(Events of Default)* of the CTA.

"SWS Financing Group" means SWSGH, SWSH, SWS, the Issuer and any other Permitted Subsidiaries.

“SWS Pension Schemes”	means the Southern Water Pension Scheme and the Southern Water Executive Pension Scheme.
“SWS Preference Share Conversion Event”	means an exercise of a Conversion Option as defined in SWS’ articles of association.
“SWS Preference Share Deed”	means the deed entered into by among others, the initial holders of the SWS Preference Shares and the Security Trustee.
“SWS Preference Shares”	means the Class A1 Preference Shares, the Class A2 Preference Shares and the Class B Preference Shares.
“SWS Preference Shareholders”	means the holders of the SWS Preference Shares from time to time.
“SWS VAT Group”	means the VAT group registration comprising SWI, SWS and SWC of which SWS is the representative member.
“SWS Water Resources Strategy”	means the water resources strategy that SWS has developed for the next 25 years, which was audited by an Ofwat reporter and submitted for approval to Ofwat and the EA.
“**SWSG**”	means Southern Water Services Group Limited, a company incorporated under the laws of England and Wales (registered number 0437 4956). and the holding company of the SWS Financing Group.
“**SWSGH**”	means SWS Group Holdings Limited.
“**SWSH**”	means SWS Holdings Limited.
“SWS/SWSG Debt Service Distribution”	means any Distribution or payment in respect of a Permitted Tax Loss Transaction to be made by SWS for the purpose of providing SWSG with the funds required to enable SWSG to meet its scheduled payment obligations under the SWS/SWSG Loan Agreement.
“SWS/SWSG Loan”	means the principal amount outstanding under the SWS/SWSG Loan Agreement from time to time.
“SWS/SWSG Loan Agreement”	means the loan agreement entered into between the Security Trustee, SWS and SWSG on the Initial Issue Date evidencing the terms of the SWS/SWSG Loan.
“SW Tax Deed of Covenant”	means the deed of covenant entered into on the Initial Issue Date by, among others, the Security Trustee, SWI, MBIA Assurance S.A. and the Obligors.
“Talons”	means the talons (if any) appertaining to, and exchangeable in accordance with the provisions therein contained for further Coupons appertaining to, the Definitive Bonds (other than Zero Coupon Bonds) and includes any replacements for Talons issued pursuant to Condition 14 *(Replacement of*

Bonds. Coupons, *Receipts and Talons).*

"Talonholders" means the several persons who are for the time being holders of the Talons.

"TARGET Settlement Day" has the meaning given to such term in Condition 6(i) *(Definitions)* as set out in Chapter 8 *"The Bonds"*.

"Tax" means any tax, levy, impost, duty or other charge or withholding of a similar nature (including any related penalty or interest) and **"Taxes", "taxation", "taxable"** and comparable expressions will be construed accordingly.

"Tax Deeds of Covenant" means the Shareholder Tax Deed of Covenant and the SW Tax Deed of Covenant.

"TDC Breach" means any breach of any covenant or representation given by, or other obligation imposed upon, any person in either of the Tax Deeds of Covenant which is considered to constitute a TDC Breach, in accordance with the terms of the relevant Tax Deed of Covenant (which, among other things, prevents a breach being a TDC Breach unless it causes, or could reasonably be expected to cause, a Material Adverse Effect).

"Temporary Global Bond" means in relation to any Sub-Class of Bearer Bonds a temporary global bond in the form or substantially in the form set out in Schedule 2, Part A to the Bond Trust Deed together with the copy of the applicable Final Terms annexed thereto, with such modifications (if any) as may be agreed between the Issuer, the Principal Paying Agent, the Bond Trustee and the relevant Dealer(s), comprising some or all of the Bearer Bonds of the same Tranche, issued by the Issuer pursuant to the Dealership Agreement or any other agreement between the Issuer and the relevant Dealer(s) relating to the Programme, the Agency Agreement and the Bond Trust Deed.

"Test Period" means:

(a) the period of 12 months ending on 31 March in the then current year;

(b) the period of 12 months starting on 1 April in the same year;

(c) each subsequent 12 month period up to the Date Prior; and

(d) if the Calculation Date falls within the 13 month period immediately prior to the Date Prior, the 12 month period from the Date Prior"

"Third Issue Date" means 27 May 2005.

"Third Issuer/SWS Loan Agreement"	means the loan agreement entered into between the Issuer and SWS on 27 May 2005.
"Tranche"	means all Bonds which are identical in all respects (save for the Issue Date, Interest Commencement Date and Issue Price).
"Transaction Documents"	means: (a) a Finance Document; (b) a Material Capex Agreement or a Material O&M Agreement; and (c) any other document designated as such by the Security Trustee and the Issuer.
"Transfer Agent"	means Deutsche Bank AG London under the Agency Agreement, including any Successor thereto.
"**Transfer Scheme**"	means a transfer scheme under Schedule 2 of the WIA.
"Treasury Transaction"	means any currency or interest rate purchase, cap or collar agreement, forward rate agreement, interest rate agreement, interest rate or currency or future or opinion contract, foreign exchange or currency purchase or sale agreement, interest rate swap, currency swap or combined similar agreement or any derivative transaction protecting against or benefiting from fluctuations in any rate or price.
"Trigger Credit Rating"	means each credit rating identified as such in Chapter 7 *"Summary of Financing Agreements" under "Trigger Events"*.
"Trigger Event"	means any of the events or circumstances identified as such in Chapter 7 *"Summary of the Financing Agreements" under "Trigger Events"*
"**Trigger Event Consequences"**	means any of the consequences of a Trigger Event identified as such in Chapter 7 *"Summary of the Financing Agreements" under "Trigger Event Consequences"*.
"Trigger Event Ratio Levels"	means the financial ratios set out in Chapter 7 *"Summary of Financing Agreements" under "Trigger Events: Financial Ratios"*.
"Trigger Event Remedies"	means any remedy to a Trigger Event as identified in Chapter 7 *"Summary of Financing Agreements" under "Trigger Events: Remedies"*.
"UAM Plan"	means Underground Asset Management Plan.
"UK"	means the United Kingdom.

"UK Listing Authority" or **"UKLA"**	means the Financial Services Authority in its capacity as competent authority under the FSMA.
"Unrestricted Chargor"	means each of SWSH and SWSGH and any other entity which accedes to the Security Agreement pursuant to Clause 27.3 *(Assignments and Transfers)* thereof that is not restricted by its regulatory or statutory obligations from providing guarantees to any other entity.
"Unrestricted Secured Liabilities"	means all present and future obligations and liabilities (whether actual or contingent and whether owed jointly or severally or in any other capacity whatsoever) of each Unrestricted Chargor to any Secured Creditor under each Finance Document to which such Unrestricted Chargor is a party, except for any obligation which, if it were secured under the Security Agreement, would result in a contravention of Section 151 of the Companies Act 1985.
"Unwrapped Debt" or **"Unwrapped Bond"**	means any indebtedness or bond (respectively) that does not have the benefit of a guarantee from a Financial Guarantor.
"Unwrapped Bondholders"	means the holders for the time being of the Unwrapped Bonds and **"Unwrapped Bondholder"** shall be construed accordingly.
"VAT"	(a) in respect of any Finance Lease Document, has the meaning given thereto in such Finance Lease Document; and (b) otherwise, means value added tax as imposed by the Value Added Tax Act 1994 and legislation supplemental thereto and other tax of a similar Fiscal nature whether imposed in the United Kingdom (instead of, or in addition to, VAT) or elsewhere.
"Voted Qualifying Class A Debt"	means the aggregate Outstanding Principal Amount of Class A Debt voted by the Class A DIG Representatives in accordance with the applicable provisions of the STID as part of the Class A DIG
"Voted Qualifying Class B Debt"	means the aggregate Outstanding Principal Amount of Class B Debt voted by the Class B DIG Representatives in accordance with the applicable provisions of the STID as part of the Class B DIG
"Water Act"	means the United Kingdom Water Act 2003.
"WIA"	means the United Kingdom Water Industry Act 1991 (as amended by subsequent legislation, including the Competition and Service (Utilities) Act 1992 and the WIA 99).

"WIA 99"	means the United Kingdom Water Industry Act 1999.
"WRA"	means the United Kingdom Water Resources Act 1991, as amended by subsequent legislation including the United Kingdom Environment Act 1995.
"Wrapped Debt" or **"Wrapped Bond"**	means any indebtedness or bond (respectively) that has the benefit of a guarantee from a Financial Guarantor.
"Wrapped Bondholders"	means the holders for the time being of the Wrapped Bonds and **"Wrapped Bondholder"** shall be construed accordingly.
"WSRA"	means the Water Services Regulation Authority.
"Zero Coupon Bond"	means a Bond specified as such in the relevant Final Terms and on which no interest is payable.

REGISTERED OFFICE OF THE ISSUER

P.O. Box 309GT
Ugland House
South Church Street
George Town, Grand Cayman
Cayman Islands

REGISTERED OFFICE OF SWS, SWSH and SWSGH

Southern House
Yeoman Road
Worthing, West Sussex BN13 3NX

BOND TRUSTEE AND SECURITY TRUSTEE

Deutsche Trustee Company Limited
Winchester House
1 Great Winchester Street
London EC2N 2DB

PRINCIPAL PAYING AGENT, TRANSFER AGENT AND AGENT BANK

Deutsche Bank AG, London Branch
Winchester House
1 Great Winchester Street
London EC2N 2DB

REGISTRAR

Deutsche Bank Luxembourg
Deutsche Bank Luxembourg S.A.
2 boulevard Konrad Adenauer
L-1115 Luxembourg

REGISTERED OFFICE OF MBIA UK INSURANCE LIMITED

1 Great St. Helen's
London EC3A 6HX

LEGAL ADVISERS

To the Issuer, SWS, SWSH and SWSGH as to English law

Linklaters
One Silk Street
London EC2Y 8HQ

To the Co-Arrangers, the Dealers, the Bond Trustee and the Security Trustee as to English law

Clifford Chance Limited Liability Partnership
10 Upper Bank Street
London E14 5JJ

To MBIA as to English law

Clifford Chance Limited Liability Partnership
10 Upper Bank Street
London E14 5JJ

To the Issuer as to Cayman Islands law

Maples and Calder

7 Princes Street

London EC2M 8AQ

AUDITORS

To the Issuer, SWS, SWSH and SWSGH

PricewaterhouseCoopers LLP

1 Embankment Place

London WC2N 6RH

To MBIA

PricewaterhouseCoopers LLP

32 London Bridge Street

London SE1 9SY

DEALERS

The Royal Bank of Scotland plc

135 Bishopsgate

London EC2M 3UR

Citigroup Global Markets Limited

Citigroup Centre

Canada Square

Canary Wharf

London E14 5LB

Credit Suisse Securities (Europe) Limited

One Cabot Square

Canary Wharf

London E14 4QJ

Morgan Stanley & Co. International Limited

25 Cabot Square

Canary Wharf

London E14 4QA