



**Northumbrian Water Finance Plc**

*(Incorporated in England and Wales with limited liability)*

**£300,000,000**

**1.625 per cent. Guaranteed Bonds due 2026**

Guaranteed by

**Northumbrian Water Limited**

*(Incorporated in England and Wales with limited liability)*

Issue price: 99.764 per cent.

The Bonds will mature on 11 October 2026. The Bonds will be issued in bearer form in denominations of £100,000 and integral multiples of £1,000 in excess thereof, up to and including £199,000. See "Terms and Conditions of the Bonds — Form, Denomination and Title". Interest on the Bonds will be payable annually in arrear on 11 October in each year, on their outstanding principal amount, with the first such payment being due on 11 October 2017. Payments of principal, any premium and interest on the Bonds will be made without withholding or deduction of United Kingdom taxes unless such withholding or deduction is required by law, as more fully described under "Terms and Conditions of the Bonds - Taxation".

The Bonds may not be redeemed prior to 11 October 2026, except as mentioned below. Northumbrian Water Finance Plc (the "Issuer") may, at its option, redeem the Bonds in whole, but not in part, at any time at a price which shall be the higher of their outstanding principal amount and an amount calculated by reference to the yield on the relevant United Kingdom government stock together with accrued interest, as more fully described under "Terms and Conditions of the Bonds — Redemption at the option of the Issuer". The Issuer may, at its option, redeem the Bonds in whole, but not in part, at their outstanding principal amount plus any interest accrued to but excluding the date of redemption for taxation reasons as described under "Terms and Conditions of the Bonds — Redemption and Purchase — Redemption for taxation reasons". Upon the occurrence of certain events as described under "Terms and Conditions of the Bonds - Redemption and Purchase - Redemption at the option of the Bondholder on a Put Event", the holder of a Bond may require the Issuer to redeem or purchase or procure the purchase of its Bonds at their outstanding principal amount plus any accrued interest.

Application has been made to the Financial Conduct Authority in its capacity as competent authority (the "UK Listing Authority") under the Financial Services and Markets Act 2000 (the "FSMA") for the Bonds 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 the Bonds to be admitted to trading on the London Stock Exchange's Regulated Market (the "Market"). References in this Prospectus to Bonds being "listed" (and all related references) shall mean that the Bonds have been admitted to trading on the Market and have been admitted to the Official List. The Market is a regulated market for the purposes of Directive 2004/39/EC of the European Parliament and of the Council on markets in financial instruments.

The Bonds will initially be represented by a temporary global bond (the "Temporary Global Bond") to be deposited on or about 11 October 2016 (the "Issue Date") with a common depositary for Euroclear Bank S.A./N.V. ("Euroclear") and Clearstream Banking, S.A. ("Clearstream, Luxembourg"). Interests in the Temporary Global Bond will be exchangeable for interests in a permanent global bond (the "Permanent Global Bond") without interest coupons attached, on or after a date which is expected to be 21 November 2016 upon certification as to non-U.S. beneficial ownership. Interests in the Permanent Global Bond will be exchangeable for definitive Bonds only in the limited circumstances set out therein.

The Bonds are expected to be rated BBB+ by Standard & Poor's Credit Market Services Europe Limited and Baa1 by Moody's Investors Service Ltd. A rating is not a recommendation to buy, sell or hold securities and may be subject to suspension, reduction or withdrawal at any time by the assigning rating agency. Standard & Poor's Credit Market Services Europe Limited and Moody's Investors Service Ltd. are established in the European Union and are registered under Regulation (EC) No. 1060/2009, as amended.

**Prospective investors should have regard to the factors described under the section headed "Risk Factors" in this Prospectus. This Prospectus does not describe all of the risks of an investment in the Bonds.**

**RBC Capital  
Markets**

**Barclays**

**Lloyds Bank**

**The Royal Bank  
of Scotland**

**Bank of China**

*This Prospectus comprises a prospectus for the purposes of Article 5 of Directive 2003/71/EC, as amended (the “**Prospectus Directive**”) and for the purpose of giving information with regard to the Issuer, Northumbrian Water Limited (the “**Guarantor**”) and the Guarantor’s subsidiaries taken as a whole (collectively, the “**Group**”) and the Bonds which, according to the particular nature of the Issuer, the Guarantor 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 the Guarantor and of the rights attaching to the Bonds.*

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

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

*To the fullest extent permitted by law, neither the Managers (as defined below) nor The Law Debenture Trust Corporation p.l.c. (the “**Trustee**”) accept any responsibility whatsoever for the contents of this Prospectus or for any other statement, made or purported to be made by a Manager or the Trustee or on its behalf in connection with the Issuer, the Guarantor or the issue and offering of the Bonds. Each Manager and the Trustee accordingly disclaims all and any liability whether arising in tort or contract or otherwise (save as referred to above) which it might otherwise have in respect of this Prospectus or any such statement.*

*This Prospectus and any other information supplied in connection with the offering of the Bonds (a) is not intended to provide the basis of any credit or other evaluation and (b) should not be considered as constituting an offer of, or an invitation by or on behalf of the Issuer, the Guarantor, or any of Barclays Bank PLC, Lloyds Bank plc, RBC Europe Limited, The Royal Bank of Scotland plc (the “**Joint Lead Managers**”) and Bank of China Limited, London Branch (together with the Joint Lead Managers, the “**Managers**”) or the Trustee to subscribe or purchase, any of the Bonds. The distribution of this Prospectus and the offering of the Bonds in certain jurisdictions may be restricted by law. Persons into whose possession this Prospectus comes are required by the Issuer, the Guarantor and the Managers to inform themselves about and to observe any such restrictions. For a description of certain further restrictions on offers and sales of Bonds and distribution of this Prospectus, see “Subscription and Sale” below.*

*No person is or has been authorised by the Issuer, the Guarantor, the Managers or the Trustee to give any information or to make any representation not contained in this Prospectus and any information or representation not so contained must not be relied upon as having been authorised by or on behalf of the Issuer, the Guarantor, any of the Managers or the Trustee. Neither the delivery of this Prospectus nor any sale or allotment made in connection with the offering of the Bonds shall, under any circumstances, constitute a representation or create any implication that there has been no change in the affairs of the Issuer, the Guarantor or the Group since the date hereof.*

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

- (i) have sufficient knowledge and experience to make a meaningful evaluation of the Bonds, the merits and risks of investing in the Bonds and the information contained or incorporated by reference in this Prospectus;*
- (ii) have access to, and knowledge of, appropriate analytical tools to evaluate, in the context of its particular financial situation, an investment in the Bonds and the impact such investment will have on its overall investment portfolio;*
- (iii) have sufficient financial resources and liquidity to bear all of the risks of an investment in the Bonds, including but not limited to, any currency exchange risk where the currency for principal or interest payments is different from the potential investor’s main operating currency;*
- (iv) understand thoroughly the terms of the Bonds and be familiar with the behaviour of the relevant indices and financial markets;*
- (v) be able to evaluate (either alone or with the help of a financial adviser) possible scenarios for economic, interest rate and other factors that may affect its investment and its ability to bear the applicable risks; and*

(vi) *have a good understanding of the water regulatory environment in the United Kingdom.*

*The Bonds have not been and will not be registered under the United States Securities Act of 1933, as amended (the “**Securities Act**”), and are in bearer form and subject to United States tax law requirements. The Bonds may not be offered, sold or delivered within the United States or to, or for the account or benefit of, U.S. persons (as defined in Regulation S) except in certain transactions exempt from the registration requirements of the Securities Act.*

In connection with the issue of the Bonds, Barclays Bank PLC as stabilising manager (the “**Stabilising Manager**”) (or any person acting on behalf of the Stabilising Manager) may over-allot Bonds or effect transactions with a view to supporting the market price of the Bonds at a level higher than that which might otherwise prevail. However, stabilisation action may not necessarily occur. Any stabilisation action may begin on or after the date on which adequate public disclosure of the terms of the offer of the Bonds is made and, if begun, may cease at any time, but it must end no later than the earlier of 30 days after the issue date of the Bonds and 60 days after the date of the allotment of the Bonds. Any stabilisation action or over-allotment must be conducted by the Stabilising Manager (or any person acting on behalf of the Stabilising Manager) in accordance with all applicable laws and rules.

*References in this document to “**pounds sterling**”, “**Sterling**” and “**£**” are to the currency of the United Kingdom, references in this document to “**euro**”, “**EUR**” and “**€**” are to the currency introduced at the start of the third stage of European economic and monetary union, and as defined in Article 2 of Council Regulation (EC) No.974/98 of 3 May 1998 on the introduction of the euro, as amended, and references in this document to “**USD**” and “**US Dollars**” are to the currency of the United States.*

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## **Documents Incorporated by Reference**

This Prospectus should be read and construed in conjunction with the unconsolidated audited financial statements of the Guarantor for the financial year ended 31 March 2016 and the financial period ended 31 March 2015, and the unconsolidated audited financial statements of the Issuer for the financial year ended 31 March 2016 and the financial period ended 31 March 2015, including in each case the audit report thereon, which have been previously published and filed with the Financial Conduct Authority. Such documents shall be deemed to be incorporated in, and form part of this Prospectus, save that any statement contained 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 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. Any document itself incorporated by reference in any document incorporated by reference in this Prospectus shall not form part of this Prospectus.

Copies of the documents incorporated by reference in this Prospectus can be obtained from the registered office of the Issuer and the Guarantor. Requests for such documents should be directed to either the Issuer or the Guarantor (as applicable) at its registered office set out at the end of this Prospectus.

## **Risk Factors**

*Prospective investors should note that the following factors may affect (as applicable) the Issuer's and the Guarantor's ability to fulfil their obligations under the Bonds and the Trust Deed and that investors could lose some or all of their investment. All of these factors are contingencies which may or may not occur and no view is expressed on the likelihood of any such contingency occurring.*

*Factors which may be material for the purpose of assessing the market risks associated with the Bonds are also described below.*

*Each of the Issuer and the Guarantor believes that the factors described below represent the principal risks inherent in investing in the Bonds, but prospective investors should note that either the Issuer or the Guarantor may be unable to pay interest, principal or other amounts on or in connection with the Bonds for other reasons and no representation is made that the statements below regarding the risks of holding any Bonds are exhaustive. Prospective investors should also read the detailed information set out elsewhere in this Prospectus (including any documents deemed to be incorporated by reference herein) and reach their own views prior to making any investment decision.*

### **Issuer's ability to fulfil its obligations under the Bonds and the Trust Deed**

The Issuer is a special purpose finance vehicle that has no assets or operations of its own and so is wholly reliant on funds it receives from the Guarantor to meet its obligations under the Bonds and the Trust Deed. The Guarantor will receive the proceeds from the issue of the Bonds.

### **Factors that may affect the Guarantor's ability to fulfil its obligations under the Bonds and the Trust Deed**

#### ***Regulatory considerations***

*Changes in law or regulation and decisions by governmental bodies and the regulators*

The Guarantor is a "relevant undertaker" (as defined in section 219(1) of the Water Industry Act 1991) and as such is regulated by the Secretary of State for Environment, Food and Rural Affairs (the "**Secretary of State**"), the Environment Agency, the Water Services Regulation Authority ("**OFWAT**") and the Drinking Water Inspectorate (as amended from time to time).

Changes in law or regulation or regulatory policy in England and Wales could materially adversely affect the Guarantor. Decisions or rulings of any of the Environment Agency, OFWAT, the Drinking Water Inspectorate or changes in UK policy could have a material adverse effect on the Guarantor's business, financial condition and results of operations as well as its ability to develop its business in the future.

The water sector in England and Wales is being opened to third party access arrangements and in the longer term there may be further changes to industry structure. There can be no assurance that these developments will not adversely affect the business or risk profile of the Guarantor.

#### ***Risk of loss of Instrument of Appointment and Special Administration Order***

The right to conduct the business of the Guarantor and to charge customers derives from the Guarantor's Instrument of Appointment. The Guarantor's Instrument of Appointment may be terminated upon 25 years' notice. No such notice has been issued to date and the Guarantor is not aware of any intention by the Secretary of State to issue such a notice.

In certain circumstances, the Secretary of State or OFWAT (with the consent of the Secretary of State) may petition the High Court to make a special administration order in relation to the Guarantor. These circumstances include where: (a) the Guarantor contravenes, or is likely to contravene, any principal duty (including its duty under section 37 of the Water Industry Act 1991 to develop and maintain an efficient and economical system of water supply within its area and its duty under section 94 of that Act to provide, improve, maintain and extend its system of public sewers) as is serious enough to make it inappropriate enough for the Guarantor to continue to hold its Instrument of Appointment; or (b) the Guarantor contravenes, or is likely to contravene, any enforcement order as is serious enough to make it inappropriate enough for the Guarantor to continue to hold its Instrument of Appointment; or (c) the Guarantor is unable, or is unlikely to be able to, to pay its debts; or (d) the Secretary of State has given certain certifications relating to the winding up of the Guarantor; or (e) the Guarantor is unable, or unwilling, to adequately participate in certain arrangements certified by the Secretary of State.

A special administration order is an order of the High Court that directs that, during the period for which the order is in force, the affairs, business and property of the Guarantor shall be managed by a person appointed by the High Court. The purposes of a special administration order are to transfer to one or more regulated companies as a going concern as much of the Guarantor's undertaking as is necessary to ensure that the functions which have been vested in the Guarantor by virtue of its Instrument of Appointment may be properly carried out. It is not certain whether or not the obligations under the Guarantee are necessary to the Guarantor's functions as a water and sewerage undertaker under its Instrument of Appointment and would, therefore, be transferred to a new company under a transfer scheme. Any such transfer scheme may, accordingly, have a material adverse effect on the Guarantor's business, financial condition and results of operation and, consequently, its ability to fulfil its obligations under the Guarantee.

*The "Water for Life" White Paper and the Water Act 2014 and impact on competition in the industry*

The "Water for Life" white paper (the "**White Paper**") was published by the United Kingdom Government on 8 December 2011 and put forward several proposals to amend the regulatory structure for the water sector in England and Wales in order to address the growing pressure on water resources in the UK and to increase competition in the sector.

The Water Act 2014, which received Royal Assent on 14 May 2014, amends the Water Industry Act 1991, as well as other legislation. The Water Act 2014 sets out the framework for some of the market reforms proposed in the White Paper but most of the changes will only apply as from a date specified by the Secretary of State (or Welsh Ministers in Wales) and secondary legislation needs to be laid before Parliament before the reforms have effect. The reforms aim to make it easier for non-domestic users to switch their water suppliers and to open up the water and sewerage market to new companies. A cross-border English-Scottish market will also be established.

The relevant reforms in the Water Act 2014 are focused on two key areas:

- *Retail competition (non-household)* – the reformed retail market is due to commence in England in April 2017 for non-household customers (businesses, charities and public sector). This stage of retail reform will allow all non-household customers to be able to switch water supplier. This represents a potential future risk of a reduced customer base for the Guarantor and could have an adverse effect on the Guarantor's business, financial condition and results of operation. The reforms will also make it easier for new entrant companies to enter the market and will allow incumbent companies to stop providing retail services to customers and exit the non-household retail market. To the extent that competition is increased within the water and sewerage services markets, this could result in a reduced customer base and market share for the Guarantor and could therefore have an adverse effect on its business, financial condition and results of operation. In July 2016 OFWAT published and consulted on emerging findings on the costs and benefits of extending retail competition in England to residential customers. The final report was published on the OFWAT website on 19 September 2016, together with supporting documents available, and sets out their final assessment of the costs and benefits.

The Department for Environment, Food and Rural Affairs ("**DEFRA**") completed a consultation on retail exit reforms in February 2015 and consulted on draft regulations to allow retail exit. The Secretary of State laid the draft Water and Sewerage Undertakers (Exit from Non-household Retail Market) Regulations 2016 before Parliament in May 2016. The regulations were made on 14 July 2016 and will come into force so as to allow the submission of exit applications from 3 October 2016 to allow retail exits to take place from the retail market opening in April 2017.

- *Upstream competition* – the upstream end of the supply chain relates to the supply of raw or treated water into a company's network or the removal of waste water or sewage for treatment. Once implemented, the reforms will enable new entrants to provide upstream services without being obliged to also provide retail services, thus introducing more potential for competition. The Government has suggested that it would not implement changes until around 2019, once work was completed on wider abstraction (removal of water from water sources) reform.

In November 2015, the Government announced that it will also seek to extend retail competition to domestic customers in England. This forms part of the HM Treasury's wider plan to look for new ways to promote open and competitive markets set out in its report "A better deal: boosting competition to bring down bills for families and firms".

The White Paper also proposed the introduction of social tariffs and also the introduction of water trading incentives. The Government published guidance in relation to social tariffs in June 2012 ("Company Social Tariffs: Guidance to water and sewerage undertakers and the Water Services Regulation Authority

under Section 44 of the Flood and Water Management Act 2010"). The water trading incentives were introduced in the 2014 price review.

Legislation will be required to implement further regulation of water quality based on a new catchment area management approach, pollution prevention measures and to introduce a new abstraction regime. These changes to the abstraction regime were consulted on in 2013, and the Government's response ("UK Government response to consultation on reforming the Water Abstraction Management System") was published on 15 January 2016. The new regime in respect of water abstraction is intended to be in place by the early 2020s.

There can be no assurance that the developments described above will not adversely affect the Guarantor's business, financial condition and results of operation and, consequentially, its ability to fulfil its obligations under the Guarantee.

#### *Potential risk of enforcement action*

The Guarantor must comply with the laws, regulations and regulatory standards applicable to its activities. Under section 22A of the Water Industry Act 1991, OFWAT and the Secretary of State (or the National Assembly for Wales in the case of Wales) may impose financial penalties on water and sewerage companies where the company is in breach of its statutory and licence obligations or where the company has caused or contributed to a contravention by a person holding a water supply licence or sewerage licence.

The maximum penalty that can be imposed is 10 per cent. of a company's turnover. There are notice requirements that must be complied with before a penalty is imposed and the company has the opportunity to make representations and objections (which the enforcement authority is required to consider). An appeal against the imposition of a penalty (including the amount thereof and the date on which it is due to be paid) lies to the High Court. There are time periods and other administration processes that apply in respect of the appeal process. If a penalty has not been paid by the due date, the enforcement authority may recover the penalty as a civil debt, including interest.

Enforcement action is potentially likely to be taken by OFWAT or the Secretary of State (or the National Assembly for Wales in the case of Wales) against water and sewerage companies only in the event of serious or persistent breaches, but a fine of this level on the Guarantor could have a material adverse effect on its results of operations in the relevant year.

#### *Price Control and Price Determination risk*

OFWAT carries out a review determining the water industry's price limits and expenditure plans every five years (a "**Periodic Review**") in respect of five year regulatory planning cycles, known as Asset Management Plan ("AMP") periods. AMP5 ended on 31 March 2015 and AMP6 started on 1 April 2015 and ends on 31 March 2021 ("**PR14**").

The current price determination set pursuant to the latest Periodic Review described in the "Northumbrian Water Limited - Business Overview" section of this Prospectus is for the period 2015 to 2020, and OFWAT is expected to determine price limits for the 2020 – 2025 period in 2019 ("**PR19**").

OFWAT has a duty to ensure, *inter alia*, that a water and sewerage company is able (in particular, by securing reasonable returns on their capital) to finance the proper carrying out of those functions.

During each Periodic Review period, OFWAT sets operating and capital cost savings. In the event that these cost savings are not achieved, the profitability of the Guarantor could be adversely affected. As a large number of the Guarantor's operating costs (for example, energy and abstraction charges) are subject to external fluctuations, this could result in the Guarantor having to achieve a greater level of operating efficiencies in other areas, which could adversely impact on regulatory targets and service levels.

As part of the AMP6 process, OFWAT has set separate, binding revenue caps for water wholesale and wastewater wholesale activities (based on an "average cost to serve") and non-household retail activities (where "default tariffs" are set to protect customers who do not or are not able to switch).

Key features of the regulatory regime for AMP6 include:

- *Greater flexibility to spend money where it is most needed.* In previous AMPs, approved expenditure was split between capital expenditure ("**Capex**"), to meet long term investment needs, or operating expenditure ("**Opex**"), to meet day-to-day running costs. The ability to earn a return on Capex under AMP5 arguably incentivised companies to seek Capex solutions to issues, even if Opex might be more efficient. In AMP6, OFWAT has considered expenditure on a total expenditure ("**Totex**") basis, removing the Capex bias so companies are encouraged to choose the most sustainable, cost effective and innovative solutions to meet their commitments.



Companies are also incentivised to outperform the Totex expenditure limits through a gain sharing incentive mechanism where companies are allowed to retain a proportion of any efficiency gains and customers benefit from lower bills in the future.

- *Aligning the interests of customers and investors.* In AMP6, company performance is measured against metrics known as Outcome Delivery Incentives (“ODIs”). While failure to achieve targets can lead to penalties, as in previous AMPs, many of these ODIs also include incentives for companies to outperform. OFWAT encouraged companies to set high level outcomes and performance commitments, in consultation with their customers and stakeholders. ODIs are based on what the customers advised was important to them, outperformance means that both customers and companies benefit. OFWAT has imposed an overall cap and collar on ODIs of plus 2 per cent. or minus 2 per cent. of the return on regulated equity.
- *A better environment.* Several ODIs are designed to deliver important environmental improvements, such as better river water quality, which focuses companies on achieving their environmental commitments over the next five years.
- *Reduced bills for customers.* While customers must be willing and able to pay for the costs of the programmes the Guarantor will deliver during AMP6, they will benefit from rising standards as well as an average reduction in bills of 5 per cent. across the industry. Water companies are also required to be doing substantially more to help people who struggle to pay their bills, for example by improving the social tariffs they offer.

Due to the intended introduction of retail competition for non-household customers in April 2017, the current determination sets out the non-household retail price control that will operate between 1 April 2015 and 31 March 2017 only. In May 2016, OFWAT published its “Business retail price review 2016: Statement of method and data table requirements”, which builds on previous publications and sets out OFWAT’s approach to the review of the business retail price control, including its intention to set the next business retail price control for a duration of three years. On 15 September 2016, OFWAT published its draft determination for the business retail price control. In its draft determination, OFWAT found that the Guarantor’s proposals were not supported by sufficient evidence and hence OFWAT has retained the PR14 price caps that apply to customers using less than 50 mega litres of water per year. The Guarantor can make further representations to OFWAT before 28 October 2016 and OFWAT will consider these in formulating its final determinations (to be published on 15 December 2016).

#### *Future Periodic Review and PR14 reconciliation*

OFWAT intends to consult on the next Periodic Review in June or July 2017, and set final price limits in December 2019. This Periodic Review will include adjustments to take account of past performance and incentive mechanisms. On 17 February 2016, OFWAT published its “PR14 reconciliation rulebook”. The rulebook is intended to provide clarity on how OFWAT expects to make adjustments to revenue and regulatory capital value (“RCV”) to reflect companies’ performance during 2015 - 2020 and how OFWAT will close out remaining PR09 reconciliation adjustments. It includes the following mechanisms: ODIs, which provide companies with rewards for achieving performance targets and compensate customers if performance is below performance targets; wholesale total expenditure sharing, where a company’s over and underperformance is shared with customers; wholesale revenue forecasting incentive mechanism, which provides financial incentives for companies to provide accurate forecasts, and ensures under- and over-recovery is reconciled; PR09 reconciliation (blind year adjustments); and household retail, where the total revenue allowance is adjusted for actual customer numbers.

In OFWAT’s PR14 final determinations, OFWAT highlighted an error in the form of an inconsistency in the calculation of the adjustments to be made to the RCVs following the operation of the of the CIS incentive mechanism during the period 2010 – 2015.

OFWAT set out the options it considered for addressing the issue in its final determinations. It decided not to make the adjustment in the final determinations, as it risked undermining regulatory predictability, which would not be in the long-term interests of customers. OFWAT considered that maintaining confidence in the regulatory framework was important in delivering benefits for customers. It made this decision in the round, taking account of the RCV adjustment that companies received through the 2010 - 2015 true-up and allowing investors a reasonable return. OFWAT indicated that it would consult as soon as was practicable on what approach should be adopted in calculating the RCV at PR19. Consistent with this commitment, it consulted in March 2015 on its preferred option for addressing the CIS reconciliation issue. Under the preferred option, the RCV, from April 2020, would reflect the actual capital expenditure rather than be inflated as a result of the inconsistent use of indexation in the models used to derive the RCV adjustment.

This would lead to a one-off change to the RCV for all companies. At an industry level, this would equate to around 2 per cent. of the RCV, but the exact adjustment for each company will vary according to its actual capital expenditure.

Future Periodic Reviews and the PR14 reconciliation may adversely affect the business of the Guarantor and its ability to perform its obligations under the Guarantee.

#### *Cost of Debt and PR19 consultation*

On 6 September 2016, OFWAT published a consultation titled “Water 2020: consultation on the approach to the cost of debt PR19”. The consultation follows from PR14 where OFWAT indicated that it would look at alternative approaches to the way it could set the cost of debt allowance in future Periodic Reviews. The consultation sets out a range of options and OFWAT’s preferred approach to the way it will set the cost of debt allowance for PR19 and also discusses alternative approaches for setting the cost of equity for PR19. OFWAT proposes three possible approaches to setting the cost of debt allowance for PR19. These are as follows: (a) continue with the current fixed allowance system (i.e. that used in PR14) where OFWAT sets a fixed cost of debt allowance for the preceding five year period, based on the cost of debt for an “efficient notionally structured company”; (b) implement full indexation of the cost of debt, whereby the debt allowance is based on a trailing average of the cost of debt over a 10 to 20 year period; and (c) index the cost of new debt only, with embedded debt costs to be set on the same basis as option one. OFWAT has said that its preferred approach is option three, where new debt only is indexed.

The consultation closes on 17 October 2016 and OFWAT intends to set out its final proposal as part of its price review methodology consultation, which it intends to publish in July 2017.

#### *Failure to obtain an Interim Determination could adversely affect profitability*

In the event of the Guarantor being materially affected by additional costs or lower revenues, regulatory mechanisms allow the Guarantor to apply to OFWAT for price limits to be re-set through an interim determination process (the “**Interim Determination**”), either as a result of specific relevant changes in circumstances, such as a new legal obligation requiring additional capital investment, or through the “**Substantial Effect Clause**”, where the total adverse impact on the Guarantor amounts to at least 20 per cent. of its turnover. OFWAT is able to challenge these processes and therefore there can be no assurance that any such determination will be favourable or available to the Guarantor.

#### *Non-recovery of customer debt*

The Guarantor is responsible for the billing, cash collection and debt management activities for its domestic and business water and waste water customers, and the Water Industry Act 1991 prohibits the Guarantor from disconnecting domestic water supplies for non-payment. The failure to recover its debts is therefore a risk to the Guarantor and may have an adverse impact on profitability. OFWAT and DEFRA both recognise the impact of bad debt on companies. This was noted in the White Paper and there have been subsequent consultations and reports from DEFRA and OFWAT about the recovery of bad debt. On 1 September 2015, OFWAT published “Guidelines for Dealing with Household Customers in Debt” (“**Debt Guidelines**”). The Debt Guidelines attempt to draw a reasonable balance between allowing companies sufficient flexibility to devise and manage effective revenue collection systems while setting out OFWAT’s views on reasonable protections for customers. In the current price determinations made by OFWAT, OFWAT reformed its approach to bad debt. This was set out in its paper “Setting price controls for 2015-20 – final methodology and expectations for companies’ business plans”. In the current price determinations, OFWAT does not make automatic adjustments for the effects of bad debt. Instead, companies are able to seek an adjustment only if they can provide substantive evidence that their level of bad debt: (a) has a material impact on their costs; (b) is beyond management control (having taken all possible steps to control it); and (c) impacts the company in a materially different way to other companies. Hence, although the Guarantor may make an application to OFWAT for an adjustment to account for its levels of bad debt, there can be no assurance that either OFWAT would permit an adjustment or that, if permitted, the amount allowed by OFWAT will be adequate for the Guarantor, and as such there is a risk of an adverse effect on the Guarantor’s business, financial condition and results of operation.

#### *Environmental, climate change and health and safety laws or regulations*

The Guarantor is subject to an increasing number of laws and regulations relating to pollution, the reduction of carbon emissions, water quality and the protection of the environment, as well as being subject to laws and regulations in England and Wales governing health and safety matters protecting its employees and the public. These expose the Guarantor to costs and liabilities relating to the Guarantor’s operations. Although the Guarantor commits significant resources towards ensuring compliance with these laws and regulations, a major safety or environmental impact incident could expose employees,

contractors and third parties to the risk of injury or a potential adverse environmental impact, thereby exposing the Guarantor to potential liability and/or loss of reputation.

Breaches of applicable environmental or health and safety laws or regulations may expose the Guarantor to penalties, claims for financial compensation and/or adverse regulatory consequences.

Furthermore, there can be no assurance that the costs of compliance with applicable environmental standards and regulations will not increase and any such increased costs could adversely affect the Guarantor's financial performance and profitability. Separately, increased water demand, water resource availability and climate change impacts may require the Guarantor to take adaptation and mitigation measures to adapt its operations to mitigate the effects and may result in the need for new resources to be developed. Existing water infrastructure may not be adequate for the future and may be vulnerable to flooding which may necessitate additional investment. Stated regulatory policy indicates continuing mandatory developments in demand management, sustainable water use, reduction of leakage in supply, implementation of household metering, the integration of catchment management, sustainable abstraction, possible water efficiency commitments and the achievement of water quality objectives in respect of surface water and groundwater pursuant to the Water Framework Directive. There can be no assurance that the developments proposed in the Water Framework Directive and summarised above will not adversely affect the Guarantor's business, financial condition and results of operation and, consequentially, its ability to fulfil its obligations under the Guarantee.

*Contamination of water supplies could adversely affect the Guarantor's business, financial condition and results of operation*

Water supplies may be subject to contamination, emanating from naturally occurring compounds, and pollution resulting from man-made sources. Although the Guarantor has established contingency plans and incident management procedures and has controls in place in respect of water supplies, if one or more of the Guarantor's water supplies becomes contaminated and the Guarantor is unable to substitute a supply or to treat the contaminated water source adequately, there may be an adverse effect on its reputation, operating results and financial position. Some or all of the remedial costs may be recoverable through future price reviews or through insurance policies maintained by the Guarantor (although there is no guarantee that all or any of the costs associated with these risks would be covered or that coverage will continue to be available in the future). The Guarantor could also be held liable for human exposure to hazardous substances in water supplies or other environmental damage, which may adversely affect the Guarantor's business, financial condition and results of operation and, consequentially, its ability to fulfil its obligations under the Guarantee.

### ***Pension scheme liabilities***

The Group operates two defined benefit pension schemes. Northumbrian Water Pension Scheme ("NWPS" or the "Scheme"), providing benefits based on final pensionable remuneration to 1,446 active members at 31 March 2016 (31 March 2015: 1,604) and AquaGib Limited Pension Plan (AGPP), providing benefits based on final pensionable remuneration to 65 active members at 31 March 2016 (31 March 2015: 67).

The assets of the NWPS and the AGPP are held separately from those of the Group in independently administered funds.

The most recent actuarial valuation of the NWPS was at 31 December 2013. At that date, the value of assets amounted to £785.9 million and the liabilities were £946.2 million, resulting in a deficit of £160.3 million and a funding level of 83.1 per cent.

The finalisation of this valuation was deferred until November 2015, because NWL commenced a consultation with members on proposed changes to the Scheme in January 2015. The consultation concluded in September 2015 and agreed a number of changes to the original proposal.

The main changes to the scheme, which took effect from 1 January 2016, were to base benefits on career average revalued earnings (CARE) basis, changing from a final salary basis, with accrued benefits at the date of implementation to be revalued in line with CPI and future CARE accrual to be revalued at RPI, both capped at 2.5 per cent.

Recognition of the benefit changes in the actuarial valuation would have resulted in a revised deficit of £106 million at 31 December 2013. The Trustee took account of both the scheme changes and significant adverse post-valuation market movements between the valuation date and 31 March 2015 in setting its contribution strategy. The future service contribution rate jointly payable by members and the employers from 1 January 2016 is 29.4 per cent. of pensionable salaries. Members' contributions are

7.3 per cent. on average with the employers paying 22.1 per cent., including 1.5 per cent. in respect of insurance premiums and expenses. In addition, the employers committed to making deficit reduction payments of £11m per annum, commencing 1 April 2015, increasing annually by RPI.

Employer contributions of £23.2 million were paid in the year to 31 March 2016, of which £11 million related to deficit reduction, with a further £3.7 million paid on behalf of employees under a salary sacrifice arrangement.

The Scheme also has a defined contribution section which had 1,530 active members at 31 March 2016 (31 March 2015: 1,356). Members can choose to contribute either 3 per cent., 4 per cent. or 5 per cent. of salary, with employers contributing at either 6 per cent., 7 per cent. or 8 per cent. depending on the member contribution rate. The contributions paid to the defined contribution section by the Group in the year totalled £4.4 million (15 months ended 31 March 2015: £4.5 million).

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

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

The Bonds may have features which contain particular risks for potential investors. Set out below is a description of certain such features:

#### *The Bonds are subject to optional redemption by the Issuer*

The Issuer may, in the circumstances set out in the Terms and Conditions of the Bonds, redeem the Bonds prior to their stated maturity date. This early redemption feature may limit the market value of the Bonds. The market value of the Bonds is unlikely to rise substantially above the price at which they can be redeemed. In addition, depending on prevailing market conditions at the time, an investor receiving the proceeds of an early redemption of the Bonds may not be able to reinvest those proceeds in a comparable security at an effective interest rate as high as that of the Bonds.

### ***Risks related to Bonds generally***

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

#### *Meetings of Bondholders/Modification and waivers*

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

The Terms and Conditions of the Bonds also provide that the Trustee may, without the consent of Bondholders or Couponholders (subject to the provisions of the Trust Deed), agree to (i) any modification of, or to any waiver or authorisation of any breach or proposed breach of, any of the provisions of the Bonds or (ii) the substitution of another company as principal debtor under the Bonds in place of the Issuer, in each case in the circumstances described in Condition 12 of the Terms and Conditions of the Bonds.

#### *Change of law*

The Terms and Conditions of the Bonds are governed by English law. No assurance can be given as to the impact of any possible judicial decision or change to English law or administrative practice after the date of this Prospectus.

#### *Political uncertainty in the UK*

On 23 June 2016 the UK held a referendum on whether the UK should remain a member of the European Union. The UK voted to leave the European Union. The announcement of the referendum result caused significant volatility in global stock markets and currency exchange rate fluctuations that resulted in a significant weakening of the Sterling against the US Dollar, the euro and other major currencies. As a result, there are a number of uncertainties in connection with the future of the UK and its relationship with the European Union. The negotiation of the UK's exit terms is likely to take a number of years. Until the terms and timing of the UK's exit from the European Union are confirmed, it is not possible to determine the impact that the referendum, the UK's departure from the European Union and/or any related matters may have on general economic conditions in the UK and/or on the business of the Guarantor.

Investors should also note that future UK political developments, including but not limited to the UK

departure from the European Union and/or any changes in government structure and policies, could affect the fiscal, monetary and regulatory landscape to which the Guarantor is subject and also therefore its financing availability and terms. Consequently no assurance can be given that the Guarantor's operating results, financial condition and prospects would not be adversely impacted as a result.

In general, no assurance can be given that any of the matters outlined above would not adversely affect the ability of the Issuer to satisfy its obligations under the Bonds and/or the market value or liquidity of the Bonds.

#### *Integral multiples of less than £100,000*

The Bonds will be issued in denominations of a minimum of £100,000 plus one or more higher integral multiples of £1,000. It is possible that the Bonds may be traded in amounts that are not integral multiples of £100,000. In such case a holder who, as a result of trading such amounts, holds an amount which is less than £100,000 in his account with the relevant clearing system at the relevant time may not receive a definitive Bond in respect of such holding (should definitive Bonds be printed) unless such holder purchased and would a further principal amount of Bonds such that its holding amounted to at least £100,000.

If definitive Bonds are issued, holders should be aware that definitive Bonds which have a denomination that is not an integral of £100,000 may be illiquid and difficult to trade.

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

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

##### *The secondary market generally*

The Bonds will have no established trading market when issued, and one may never develop. If a market does develop, it may not be liquid. There may at any time be only one or a few investors in the Bonds. Therefore, investors may not be able to sell their Bonds easily or at prices that will provide them with a yield comparable to similar investments that have a developed secondary market. Accordingly the purchase of Bonds is suitable only for investors who can bear the risks associated with a lack of liquidity in the Bonds and the financial and other risks associated with an investment in the Bonds.

Investors must be prepared to hold the Bonds until maturity.

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

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

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

##### *Interest rate risks*

Investment in the Bonds involves the risk that subsequent changes in market interest rates may adversely affect the value of the Bonds.

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

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

In general, European regulated investors are restricted under Regulation (EC) No. 1060/2009, as amended (the "**CRA Regulation**") from using credit ratings for regulatory purposes, unless such ratings are issued by a credit rating agency established in the EU and registered under the CRA Regulation (and such registration has not been withdrawn or suspended). Such general restriction will also apply in the

case of credit ratings issued by non-EU credit rating agencies, unless the relevant credit ratings are endorsed by an EU-registered credit rating agency or the relevant non-EU rating agency is certified in accordance with the CRA Regulation (and such endorsement action or certification, as the case may be, has not been withdrawn or suspended).

*Legal investment considerations may restrict certain investments*

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

## Terms and Conditions of the Bonds

*The following is the text of the Terms and Conditions of the Bonds substantially in the form in which they will appear on the reverse of each Bond in definitive form.*

The 1.625 per cent. Guaranteed Bonds due 2026 (the “**Bonds**”, which expression shall in these terms and conditions (the “**Conditions**”), unless the context otherwise requires, include any further bonds issued pursuant to Condition 14 and forming a single series therewith) of Northumbrian Water Finance Plc (the “**Issuer**”) are issued in an aggregate principal amount of £300,000,000. The Bonds are constituted by a trust deed (the “**Trust Deed**”) dated 11 October 2016 between the Issuer, Northumbrian Water Limited (the “**Guarantor**”) and The Law Debenture Trust Corporation p.l.c. (the “**Trustee**”, which expression shall include all persons for the time being the trustee or trustees under the Trust Deed) as trustee for the holders of the Bonds (the “**Bondholders**”).

The Bonds were authorised pursuant to a resolution of the Board of Directors of the Issuer passed on 28 September 2016. The giving of the Guarantee (as defined in Condition 2) was authorised pursuant to a resolution passed on 28 September 2016 of the Standing Committee of the Board of Directors of the Guarantor established during April 2000 and ratified pursuant to a resolution of the Board of Directors of the Guarantor passed on 31 March 2011 of the Board of Directors of the Guarantor.

Certain statements hereunder are summaries of, and are subject to, the detailed provisions of the Trust Deed, which includes the form of the Bonds and the coupons appertaining thereto (the “**Coupons**”). Copies of the Trust Deed and the paying agency agreement dated 11 October 2016 (the “**Paying Agency Agreement**”), relating to the Bonds between the Issuer, the Guarantor, the Trustee and the principal paying agent and paying agents named in it are available for inspection by prior appointment during usual business hours at the registered office for the time being of the Trustee, being at the date of issue hereof at Fifth Floor, 100 Wood Street, London EC2V 7EX, United Kingdom and at the specified offices of the principal paying agent for the time being (the “**Principal Paying Agent**”) and the paying agents for the time being (the “**Paying Agents**” which expression shall include the Principal Paying Agent). The Bondholders and the holders for the time being of the Coupons (the “**Couponholders**”) are entitled to the benefit of, are bound by, and are deemed to have notice of, all provisions of the Trust Deed and are deemed to have notice of those provisions of the Paying Agency Agreement applicable to them.

### 1 Form, Denomination and Title

The Bonds are issued in bearer form in denominations of £100,000 and integral multiples of £1,000 in excess thereof up to and including £199,000, are serially numbered and are issued with Coupons attached. Title to the Bonds and Coupons will pass by delivery. No definitive Bonds will be issued with a denomination exceeding £199,000.

The Issuer, the Guarantor, any Paying Agent and the Trustee may (to the fullest extent permitted by applicable laws) deem and treat the holder of any Bond and the holder of any Coupon as the absolute owner of such Bond or Coupon for all purposes (whether or not such Bond or Coupon shall be overdue and notwithstanding any notice of ownership or writing thereon or any notice of previous loss or theft thereof) and none of the Issuer, the Guarantor, any Paying Agent and the Trustee will be liable for so treating such holder.

### 2 Guarantee and Status

#### (a) Guarantee

The Guarantor has unconditionally and irrevocably guaranteed the due payment of all sums expressed to be payable by the Issuer under the Trust Deed, the Bonds and the Coupons. Its obligations in that respect (the “**Guarantee**”) are contained in the Trust Deed.

#### (b) Status

The Bonds and Coupons constitute direct, unconditional and (subject to the provisions of Condition 3) unsecured obligations of the Issuer and rank (subject as aforesaid and to laws relating to creditors’ rights) *pari passu* and without preference among themselves. The payment obligations of the Issuer under the Bonds and Coupons and of the Guarantor under

the Guarantee shall, save for such exceptions as may be provided by applicable legislation, and subject to Condition 3, at all times rank equally with all their respective other present and future unsecured and unsubordinated obligations.

### 3 Negative Pledge

So long as any of the Bonds remain outstanding (as defined in the Trust Deed) neither the Issuer nor the Guarantor will create or permit to subsist any mortgage, charge, lien (other than a lien arising by operation of law) or other encumbrance upon the whole or any part of its undertaking or assets, present or future, to secure payment of any present or future Relevant Indebtedness (as defined below) of the Issuer or the Guarantor or to secure any guarantee or indemnity given by it in respect of any Relevant Indebtedness of any other person, without at the same time according to the Bonds, to the satisfaction of the Trustee, at least the same security as is created or subsisting to secure any such Relevant Indebtedness, guarantee or indemnity, or such other security as the Trustee shall in its absolute discretion deem not materially less beneficial to the Bondholders or as shall be approved by an Extraordinary Resolution (as defined in the Trust Deed) of the Bondholders.

“**Relevant Indebtedness**” means any indebtedness for borrowed money which is in the form of, or represented or evidenced by, bonds, notes, loan stock or other securities which, with the agreement of the issuer are quoted, listed, dealt in or traded on a stock exchange, or over the counter or other recognised securities market, other than such bonds, notes, loan stock or other securities which (i) have an initial maturity of greater than twenty years, and (ii) are denominated in sterling.

### 4 Interest

The Bonds bear interest from and including 11 October 2016 on their outstanding principal amount at the rate of 1.625 per cent. per annum. Interest shall be payable annually in arrear on 11 October in each year (each an “**Interest Payment Date**”) commencing 11 October 2017.

Interest due on or before maturity of the Bonds will be paid against presentation and surrender of the relevant Coupons in accordance with and subject to Condition 6. Interest shall cease to accrue on any Bond from and including the due date for redemption thereof unless payment of principal and any applicable premium is improperly withheld or refused whereupon interest shall continue to accrue at the rate specified in the Trust Deed both before and after judgement until the moneys have been received by the Trustee or the Principal Paying Agent and notice to that effect is given in accordance with Condition 11. If interest is required to be calculated for a period of less than one Determination Period (as defined below), it will be calculated on the basis of the number of days in the relevant period divided by the number of days in the Determination Period in which the relevant period ends and divided by the number of Determination Periods normally ending in any year. If interest is to be calculated for a period of more than one Determination Period, it will be calculated on the basis of the sum of:

- (a) the number of days in the relevant period falling in the Determination Period in which it begins divided by the number of days in such Determination Period; and
- (b) the number of days in the relevant period falling in the next Determination Period divided by the number of days in such Determination Period.

In this Condition, “**Determination Period**” means the period from, and including, 11 October in any year to, but excluding, 11 October in the immediately succeeding year.

### 5 Redemption and Purchase

- (a) *On maturity*

Unless previously redeemed or purchased and cancelled, the Bonds will be redeemed by the Issuer at their outstanding principal amount on 11 October 2026 (the “**Maturity Date**”).

- (b) *Redemption at the option of the Issuer*

The Issuer may at any time, having given not less than 30 nor more than 45 days’ notice in accordance with Condition 11, redeem all, but not some only, of the Bonds at a price (the



“**Redemption Price**”) which shall be the higher of the amounts set out in (i) and (ii) below, together with interest accrued up to and including the date of redemption:

- (i) their outstanding principal amount; and
- (ii) the price (expressed as a cash amount and rounded to the nearest penny, £0.005 being rounded upwards), at which (A) the Gross Real Yield on the Bonds, if they were to be purchased at such price on the third Business Day prior to the due date of redemption, would be equal to (B) the Gross Real Yield on such dealing day of the Reference Stock on the basis of the middle market price of the Reference Stock prevailing at 11.00 a.m. on such dealing day, as determined by an independent financial adviser (or such other person as the Trustee may approve) (an “**Independent Financial Adviser**”).

At any time when under these Conditions it is necessary to have, or the Trustee requests, the appointment of an Independent Financial Adviser, the Issuer (failing whom the Guarantor) shall select and appoint an Independent Financial Adviser with the approval of the Trustee and at the expense of the Issuer (failing whom, the Guarantor). Any reference in these Conditions to principal or outstanding principal amount shall be deemed to include any sum payable by way of the Redemption Price.

In this Condition:

“**Business Day**” means a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in London.

“**Reference Stock**” means the 1.50 per cent. Treasury Stock due July 2026 or, if such Treasury Stock is no longer in issue, such other United Kingdom government stock as the Trustee may, with the advice of three leading brokers and/or market makers operating in the gilt edged market, agree with the Issuer, or failing such agreement, decide from time to time to be appropriate.

At any time when under these Conditions it is necessary to have the advice of leading brokers and/or market makers operating in the gilt edged market, the Issuer (failing whom the Guarantor) shall select them with the approval of the Trustee and at the expense of the Issuer (failing whom, the Guarantor).

Notices of redemption will specify the date fixed for redemption and the applicable Redemption Price. Upon the expiry of any notice of redemption the Issuer (failing whom the Guarantor) shall be bound to redeem the Bonds at the applicable Redemption Price. The “**Gross Real Yield**” on the Bonds and on the Reference Stock will be expressed as a percentage and will be calculated in accordance with generally accepted market price for such time, as advised to the Issuer by the Independent Financial Adviser.

(c) *Redemption for taxation reasons*

In the event that the Issuer (or if the Guarantee were called, the Guarantor) has or will become obliged to pay additional amounts as provided or referred to in Condition 7 as a result of any change in, or amendment to, the laws or regulations of the United Kingdom or any authority thereof or therein having power to tax, or any change in the application or judicial or official interpretation of such laws or regulations (which change or amendment becomes effective on or after 7 October 2016), the Issuer (or the Guarantor, if applicable) will from the date such change becomes effective (the “**Tax Change Date**”) immediately commence, and continue for a period of six months following the Tax Change Date, to use its reasonable endeavours to have passed, by means of an Extraordinary Resolution (as defined in the Trust Deed) approved at a meeting of Bondholders held in accordance with the provisions of the Trust Deed, resolutions with the purpose of effecting:

- (i) any restructuring of the Bonds and/or the Guarantee as may be necessary to avoid the requirement to pay such additional amounts; or

- (ii) the substitution of the Issuer as principal debtor under the Bonds with another person, whether established or domiciled in the same or an alternative jurisdiction as the Issuer, as principal debtor in order to avoid the requirement to pay such additional amounts; or
- (iii) the issue of new securities, in substitution for and replacement of the Bonds, by the Issuer or another member of the Group (as defined in Condition 8), having terms and conditions resulting in the new securities being at least economically equivalent to the Bonds and the Guarantee taken together in respect of the payment of principal and interest as would have been applicable in the absence of any requirement upon the Issuer to pay such additional amounts,

and, failing the making of any of the arrangements specified in sub-paragraphs (i), (ii) or (iii) above within six months of the Tax Change Date, the Issuer may redeem (or, if applicable, the Guarantor may direct the Issuer to redeem) all, but not some only, of the Bonds at any time, on giving not less than 30 days' nor more than 60 days' notice in accordance with Condition 11 (which notice shall be irrevocable) at the outstanding principal amount thereof, together with interest accrued to the date fixed for redemption, provided that no such notice of redemption shall be given earlier than the expiry of the six month period referred to above or, if later, 90 days prior to the earliest date following the Tax Change Date on which the Issuer (or the Guarantor as the case may be) would be obliged to pay such additional amounts were a payment in respect of the Bonds (or the Guarantee, as the case may be) then due.

Prior to the publication of any notice of redemption pursuant to this Condition 5(c), the Issuer (or, as the case may be, the Guarantor) shall deliver to the Trustee a certificate signed by two directors of the Issuer (or the Guarantor as the case may be) stating that the obligation to pay additional amounts referred to above cannot be avoided by the Issuer (or the Guarantor as the case may be) using its reasonable endeavours as aforesaid and the Trustee shall be entitled to accept such certificate as sufficient evidence of the use of such reasonable endeavours without further liability to Bondholders thereof in which event it shall be conclusive and binding on the Bondholders and the Couponholders.

(d) *Redemption at the option of the Bondholder on a Put Event*

If, at any time while any of the Bonds remains outstanding, a Put Event (as defined below) occurs, then, unless at any time the Issuer shall have given a notice under Condition 5(b) or 5(c), in each case expiring prior to the Put Date (as defined below) the holder of each Bond will, upon the giving of a Put Notice (as defined below), have the option to require the Issuer to redeem or purchase or procure the purchase of the Bond on the Put Date at its outstanding principal amount, together with interest accrued up to, and including, the Put Date.

A "**Put Event**" occurs if (i) the appointment of the Guarantor (the "**Appointment**") as the water undertaker and sewerage undertaker for the areas described in the Instrument of Appointment dated 1 September 1989 made by the Secretary of State under Sections 11 and 14 of the Water Act 1989 (as in effect on 1 September 1989) as varied and modified from time to time is terminated; or (ii) a Restructuring Event (as defined below) occurs and, within the Restructuring Period (as defined below), either (a) if at the time the relevant Restructuring Event occurs there are Rated Securities, a Rating Downgrading (both as defined below) in respect of that Restructuring Event also occurs; or (b) if at such time there are no Rated Securities, the Issuer or the Guarantor fails to obtain (whether by failing to seek a rating or otherwise) a rating of the Bonds or any other unsecured and unsubordinated debt of the Issuer or the Guarantor having an initial maturity of five years or more, from a Rating Agency (as defined below) of at least investment grade (BBB-/Baa3, or its equivalent for the time being) (a "**Negative Rating Event**"), and in the case of either (a) or (b), such Restructuring Event is certified in writing by an Independent Financial Adviser as being in its opinion materially prejudicial to the interests of the Bondholders (a "**Negative Certification**") (that Restructuring Event and the relevant Rating Downgrading or, as the case may be, Negative Rating Event and, in each case, the Negative Certification together constituting the Put Event); or (iii) any Subsidiary (as defined below) of the Guarantor being, at the date of issue of the Bonds, a Material Subsidiary (as defined below) ceases to be wholly-owned by the Guarantor.

Promptly upon becoming aware that a Put Event has occurred, and in any event not later than 21 days after the occurrence of the Put Event, the Issuer shall, and at any time upon the

Trustee having express notice thereof, the Trustee may, and if so requested by the holders of at least one quarter in outstanding principal amount of the Bonds then outstanding (provided in either case it shall have been indemnified and/or secured and/or pre-funded to its satisfaction), shall, give notice (a **"Put Event Notice"**) to the Bondholders in accordance with Condition 11, specifying the nature of the Put Event and the procedure for exercising the option contained in this Condition 5(d). Any Negative Certification shall, in the absence of manifest error, be conclusive. The Trustee will be under no duty to monitor whether there has been the occurrence of a Put Event.

To exercise the option to require the Issuer to redeem or purchase or procure the purchase of a Bond under this Condition 5(d), the Bondholder must deliver such Bond, on any business day (as defined in Condition 6) falling within the period (the **"Put Period"**) of 45 days after a Put Event Notice is given, at the specified office of any Paying Agent, accompanied by a duly signed and completed notice of exercise in the form (for the time being current) obtainable from the specified office of any Paying Agent (a **"Put Notice"**). The Bond must be delivered to the Paying Agent together with all Coupons appertaining thereto maturing after the date (the **"Put Date"**) being the seventh day after the date of expiry of the Put Period, failing which such redemption or purchase, as the case may be, shall be made only against such indemnity as the Issuer may reasonably require. The Paying Agent to which such Bond and Put Notice are delivered will issue to the Bondholder concerned a non-transferable receipt (a **"Receipt"**) in respect of the Bond so delivered. Payment by the Issuer in respect of any Bond so delivered shall be made, if the holder duly specified in the Put Notice a bank account to which payment is to be made, by transfer to that bank account on the Put Date, and in every other case, on or after the Put Date against presentation and surrender of such Receipt at the specified office of any Paying Agent. A Put Notice, once given, shall be irrevocable. For the purposes of Conditions 8, 9, 11 and 12 and certain other purposes specified in the Trust Deed, Receipts issued pursuant to this Condition 5(d) shall be treated as if they were Bonds.

In these Conditions:

**"Rated Securities"** means the Bonds, if at any time and for so long as they shall have a rating from a Rating Agency, and otherwise any other unsecured and unsubordinated debt of the Guarantor having an initial maturity of five years or more which is rated by a Rating Agency.

**"Rating Agencies"** means Standard & Poor's Credit Market Services Europe Limited and Moody's Investors Service Ltd. or any of their respective successors, or any rating agency substituted for Standard & Poor's Credit Market Services Europe Limited or Moody's Investors Service Ltd. (or any permitted substitute of either of them) by the Issuer from time to time with the prior written approval of the Trustee (not to be unreasonably withheld or delayed) or any other rating agency approved in writing by the Trustee from time to time and **"Rating Agency"** means any one of them.

A **"Rating Downgrading"** shall be deemed to have occurred in respect of a Restructuring Event if the current rating assigned to the Rated Securities by any Rating Agency (whether provided by a Rating Agency at the invitation of the Issuer or by its own volition) is withdrawn or reduced from an investment grade rating (BBB-/Baa3, or its equivalent for the time being, or better) to a non-investment grade rating (BB+/Ba1, or its equivalent for the time being, or worse), or, if the Rating Agency shall have already rated the Rated Securities below investment grade (as described above), the rating is withdrawn or lowered one full rating category.

**"Restructuring Event"** means either (i) the modification of any material rights, benefits or obligations of the Guarantor as a water undertaker or sewerage undertaker arising under the Appointment or the Water Industry Act 1991 or (ii) any material modification made to the Appointment or the Scheme (being a scheme made under Schedule 2 of the Water Industry Act 1991 pursuant to which property, rights and liabilities of the water authority to which the Guarantor is the successor were transferred to the Guarantor), regardless of whether or not such modification is made with the consent of the Guarantor and whether pursuant to the Water Industry Act 1991 or otherwise or (iii) any legislation (whether primary or subordinate) is enacted removing, reducing or qualifying the duties or powers of the Secretary of State for the Environment, Food and Rural Affairs and/or the Water Services Regulation Authority (or any successor) (including without limitation any such legislation removing, reducing or qualifying

such duties or powers under or pursuant to Sections 2, 9 or 24 of the Water Industry Act 1991) in each case as compared to those in force on 7 October 2016.

**“Restructuring Period”** means, whether or not there are Rated Securities at the time a Restructuring Event occurs, the period of 45 days starting from and including the day on which a Restructuring Event occurs.

**“Subsidiary”** means, in relation to any entity, a subsidiary of such entity within the meaning of Section 1159 of the Companies Act 2006, and **“Material Subsidiary”** means any Subsidiary of the Guarantor (not being an Excluded Subsidiary as defined in Condition 8) (a) whose profits on ordinary activities before tax or whose net assets (in each case consolidated in respect of a Subsidiary which itself has Subsidiaries, and in each case attributable to the Guarantor) all as shown in the latest audited accounts (consolidated or, as the case may be, unconsolidated) of such Subsidiary represent 20 per cent. or more of the consolidated profits on ordinary activities before tax or, as the case may be, consolidated net assets (in each case attributable to the shareholders of the Guarantor) of the Guarantor and its Subsidiaries (other than Excluded Subsidiaries, as defined in Condition 8) all as shown in the latest audited consolidated accounts of the Guarantor (as adjusted); or (b) to which is transferred all or substantially all of the business, undertaking or assets of a Subsidiary which immediately prior to such transfer is a Material Subsidiary, whereupon the transferor Subsidiary shall immediately cease to be a Material Subsidiary and the transferee Subsidiary shall become a Material Subsidiary until publication of its next audited accounts when whether or not it shall continue to be a Material Subsidiary shall be determined pursuant to sub-paragraph (a). A certificate signed by two directors for the time being of the Guarantor that in their opinion a Subsidiary is or is not or was or was not at any particular time a Material Subsidiary shall, in the absence of manifest error, be conclusive and binding on all parties.

(e) *Purchase*

The Guarantor, the Issuer and any other Subsidiary of the Guarantor may at any time purchase Bonds (together with all unmatured Coupons appertaining thereto) in the open market or otherwise at any price.

(f) *Cancellation*

All Bonds which are (i) redeemed or (ii) purchased by or on behalf of the Guarantor, the Issuer or any other Subsidiary of the Guarantor will forthwith be cancelled, together with all unmatured Coupons attached thereto or surrendered therewith, and accordingly may not be reissued or sold.

## 6 Payments

Payments of principal, any premium and interest will be made against surrender of Bonds or Coupons, as the case may be, at any specified office of any Paying Agent by transfer to an account denominated in pounds sterling maintained by the payee with, a bank in London, subject in all cases to (i) any fiscal or other laws or regulations applicable thereto in the place of payment, but without prejudice to the provisions of Condition 7 and (ii) any withholding or deduction required pursuant to an agreement described in Section 1471(b) of the U.S. Internal Revenue Code of 1986 (the **“Code”**) or otherwise imposed pursuant to Sections 1471 through to 1474 of the Code, any regulations or agreements thereunder, any official interpretations thereof, or (without prejudice to the provisions of Condition 7) any law implementing an intergovernmental approach thereto. If the due date for redemption of any Bond is not an Interest Payment Date in any year, accrued interest will be paid against presentation of the relevant Bond. All payments of principal and interest shall be rounded to the nearest penny (£0.005 being rounded upwards) on the outstanding principal amount of the Bond.

If the due date for payment of any amount on any Bond or Coupon is not a business day (as defined below), then the holder thereof will not be entitled to payment of such amount until the next following business day and will not be entitled to any further interest or other payment in respect of such postponement. In this paragraph, **“business day”** means any day on which banks are open for business in London and in the place of the specified office of the Paying Agent at which the Bond or Coupon is presented for payment.

The Issuer may at any time (with the previous approval of the Trustee) vary or terminate the appointment of any Paying Agent and appoint additional or other Paying Agents, provided that it will at all times maintain (i) a Principal Paying Agent and (ii) a Paying Agent (which could be the Principal Paying Agent) with a specified office in London. Notice of any such termination or appointment and of any change in the office through which any Paying Agent will act will be given in accordance with Condition 11. Upon the due date for redemption of any Bond (or purchase pursuant to Condition 5), unmatured Coupons relating to such Bond (whether or not attached) shall become void and no payment shall be made in respect of such Coupons. Where any Bond is presented for redemption without all unmatured Coupons relating to it, redemption shall be made only against the provision of such indemnity as the Issuer may reasonably require.

## 7 Taxation

All payments of principal, any premium and interest in respect of the Bonds and the Coupons or under the Guarantee shall 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, levied, collected, withheld or assessed by or on behalf of the United Kingdom or any political subdivision thereof or any authority thereof or therein having power to levy the same unless such withholding or deduction is required by law. In that event the Issuer, or as the case may be, the Guarantor shall pay such additional amounts as will result in the receipt by the Bondholders and the Couponholders of such net amounts as would have been received by them had no such withholding or deduction been required; provided that no such additional amounts will be payable in respect of Bonds or Coupons presented for payment:

- (i) by or on behalf of a Bondholder or Couponholder who is liable for such taxes, duties, assessments or governmental charges by reason of his having some connection with the United Kingdom other than the mere holding of a Bond or Coupon; or
- (ii) by or on behalf of a Bondholder or Couponholder who would not be liable or subject to deduction or withholding by making a declaration of beneficial ownership of the Bond or Coupon and of non-residence or other similar claim for exemption to the relevant tax authority or to any relevant person; or
- (iii) more than 30 days after the Relevant Date except to the extent that a Bondholder or Couponholder would have been entitled to payment of such additional amounts if he had presented his Bond or Coupon for payment on the thirtieth day after the Relevant Date.

**“Relevant Date”** means, in respect of any payment, (a) the date on which such payment first becomes due or (b) if the full amount payable has not been received by the Principal Paying Agent or the Trustee on or prior to such date, the date on which, the full amount of such money having been so received, notice to that effect shall have been duly published in accordance with Condition 11.

In these Conditions references to **“principal”** or **“interest”** shall be deemed also to refer to additional amounts which may be payable as described above or under any obligation undertaken in addition thereto or in substitution therefor pursuant to the Trust Deed.

## 8 Events of Default

The Trustee, at its discretion may, and if so requested in writing by the holder of at least one quarter in outstanding principal amount of the Bonds then outstanding or if so directed by an Extraordinary Resolution of the Bondholders shall, in each case if indemnified and/or secured and/or pre-funded to its satisfaction, give notice to the Issuer and the Guarantor that the Bonds are, and they shall accordingly immediately become, due and repayable at their outstanding principal amount plus accrued interest as provided in the Trust Deed, if any of the following events shall occur:

- (i) if default is made for a period of 15 days or more in the payment of (a) any interest in respect of the Bonds after the due date therefor or (b) principal of or premium on the Bonds in accordance with Condition 5(d) after the due date therefor; or
- (ii) if the Issuer or the Guarantor fails to perform or observe any obligation binding on it under the Bonds or the Trust Deed (other than any obligation for payment of any principal, premium or interest in respect of the Bonds) and, except where, in the opinion of the Trustee, such default is not capable of remedy, such default continues for 30 days (or such longer period as the

Trustee may permit) after written notice thereof by the Trustee to the Issuer or the Guarantor specifying such failure and requiring the same to be remedied; or

- (iii) if (a) a petition is presented (and is not dismissed within 60 days) or an order is made or an effective resolution passed for the appointment of an administrator or the winding-up of the Issuer, the Guarantor or any Principal Subsidiary (as defined below) (except, in the case of a Principal Subsidiary, a winding-up for the purposes of a reconstruction or amalgamation, the terms of which have previously been approved in writing by the Trustee or by an Extraordinary Resolution (as defined in the Trust Deed), or voluntary solvent winding-up in connection with the transfer of all or (in the opinion of the Trustee) the major part of the business, undertaking and assets of such Principal Subsidiary to the Issuer, the Guarantor or another Subsidiary Undertaking (as defined below) of the Issuer or the Guarantor (not being an Excluded Subsidiary)); or (b) a petition is presented (and is not dismissed within 60 days) or an order is made in respect of the Guarantor pursuant to Section 24 of the Water Industry Act 1991; or
- (iv) if the Issuer, the Guarantor or any Principal Subsidiary stops or threatens to stop payment generally or ceases or threatens to cease to carry on its business or (in the opinion of the Trustee) a substantial part of its business (except, in the case of a Principal Subsidiary, a cessation or threatened cessation for the purpose of a reconstruction or amalgamation the terms of which have previously been approved in writing by the Trustee or by an Extraordinary Resolution, or in connection with the transfer of all or (in the opinion of the Trustee) the major part of the business, undertaking and assets of such company to the Issuer, the Guarantor or another of their respective Subsidiaries (not being an Excluded Subsidiary)); or
- (v) if an encumbrancer takes possession or an administrative or other receiver is appointed of the whole or (in the opinion of the Trustee) any material part of the undertaking or assets of the Issuer, the Guarantor or any Principal Subsidiary or if a distress, execution or any similar proceedings is levied or enforced upon or sued out against the whole or (in the opinion of the Trustee) any material part of the property of the Issuer, the Guarantor or any Principal Subsidiary and in any such case is not removed, paid out or discharged within 21 days (or such longer period as the Trustee may approve); or
- (vi) if the Issuer, the Guarantor or any Principal Subsidiary is unable to pay its debts generally as they fall due or suspends making payments (whether of principal or interest) with respect to all or any class of its debts or announces an intention to do so; or
- (vii) if any kind of composition, scheme of arrangement, compromise or other similar arrangement involving the Issuer, the Guarantor or any Principal Subsidiary and the creditors of any of them generally (or any class of such creditors) is entered into or made; or
- (viii) if any indebtedness for Moneys Borrowed (as defined below) having an aggregate outstanding principal amount equal to or greater than the Threshold Amount (as defined below) of the Issuer, the Guarantor or any of their respective Subsidiaries becomes or is validly declared to be due and payable prior to the date on which the same would otherwise become due and payable by reason of the occurrence of an event of default in relation thereto or any indebtedness for Moneys Borrowed of the Issuer, the Guarantor or any of their respective Subsidiaries having an aggregate outstanding principal amount equal to or greater than the Threshold Amount is not paid at the maturity thereof or at the expiry of any originally applicable grace period or any guarantee or indemnity in respect of any such indebtedness given by the Issuer, the Guarantor or any of their respective Subsidiaries shall not be paid when due and called upon or at the expiry of any originally applicable grace period save in any such case where there is a bona fide dispute as to whether payment is due; or
- (ix) if any of the obligations of the Guarantor under the Trust Deed are not (or are claimed by the Guarantor not to be) in full force and effect,

provided that in the case of any such event as is referred to in (ii) and, in relation to any Principal Subsidiary, (iii) to (vii) above, and, in relation to any Subsidiary, (viii) above, the Trustee shall first have certified in writing that such event is, in its opinion, materially prejudicial to the interests of the Bondholders.

In these Conditions:

**“Excluded Subsidiary”** means any Subsidiary (as defined in Condition 5(d)) or Subsidiary Undertaking of the Guarantor (a) which is a single purpose company whose principal assets and business are constituted by a project, (b) none of whose liabilities in respect of the financing of such project are directly or indirectly the subject of security or a guarantee, indemnity or any other form of assurance, undertaking or support from the Guarantor or any of its Subsidiaries or Subsidiary Undertakings and (c) which has been designated as such by the Guarantor by written notice to the Trustee; provided that the Guarantor may give written notice to the Trustee at any time that any Excluded Subsidiary is no longer an Excluded Subsidiary, whereupon it shall cease to be an Excluded Subsidiary. Additionally, Reiver Holdings Limited, Reiver Finance Limited, Bakethin Holdings Limited and Bakethin Finance PLC shall be Excluded Subsidiaries notwithstanding that they may otherwise not have been by virtue of the other provisions of this paragraph.

**“Group”** means the Guarantor and its Subsidiary Undertakings.

**“Moneys Borrowed”** means (a) borrowed moneys, and (b) liabilities under any bond, note, bill, debenture, loan stock or other security in each case issued (i) as consideration for assets or services (but excluding such liabilities incurred in relation to the acquisition of assets or services in the ordinary course of trading) or (ii) for cash or (iii) under acceptance credit facilities.

**“Net Tangible Assets”** at any time means the aggregate at such time of:

- (a) the nominal share capital of the Guarantor for the time being issued and paid up or credited as paid up;
- (b) any credit balance on the consolidated or, if at such time the Guarantor only produces non-consolidated accounts, the non-consolidated profit and loss account of the Guarantor; and
- (c) any other consolidated or, if at such time the Guarantor only produces non-consolidated accounts, non-consolidated capital and revenue reserves of the Guarantor (which, for the avoidance of doubt shall not include any provision for deferred tax);

less the aggregate of:

- (d) any debit balance on the consolidated or, if at such time the Guarantor only produces non-consolidated accounts, non-consolidated profit and loss account of the Guarantor;
- (e) any amounts shown in the consolidated or, if at such time the Guarantor only produces non-consolidated accounts, non-consolidated balance sheet of the Guarantor in respect of goodwill or other intangible assets of the Guarantor;
- (f) any amounts credited to any consolidated or, if at such time the Guarantor only produces non-consolidated accounts, non-consolidated revaluation reserves as a result of any writing up of book values of any assets of the Group after the date of the financial statements for the year ended 31 March 2016, other than in respect of any revaluation of any freehold or leasehold interest in real property or any plant or machinery, but only to the extent that such valuation is based on a professional valuation by a reputable valuer; and
- (g) any amounts required to be set aside for taxation payable by the Guarantor and its Subsidiaries or for any distribution declared, recommended or made by the Guarantor or any of its Subsidiaries (other than to another member of the Group), in each such case to the extent that the same is not provided for in the accounts of the Guarantor.

A certificate signed by two directors for the time being of the Guarantor as to the amount of the Net Tangible Assets at any given time shall, in the absence of manifest error, be conclusive and binding on all parties.

**“Principal Subsidiary”** means any Subsidiary Undertaking of the Guarantor (a) whose profits on ordinary activities before tax or whose net assets (in each case consolidated in respect of a Subsidiary Undertaking which itself has Subsidiary Undertakings, and in each case attributable to the Guarantor) all as shown in the latest audited accounts (consolidated or, as the case may be,

unconsolidated) of such Subsidiary Undertaking represent 10 per cent. or more of the consolidated profits on ordinary activities before tax or, as the case may be, consolidated net assets (in each case attributable to the shareholders of the Guarantor) of the Guarantor and its Subsidiary Undertakings (other than Excluded Subsidiaries) either (i) if the latest audited accounts of the Guarantor are consolidated accounts, as shown in such accounts or (ii) if the latest audited accounts of the Guarantor are non-consolidated accounts, as would be shown in the latest audited accounts of the Guarantor had such accounts been consolidated accounts, in each case, as adjusted; or (b) to which is transferred all or substantially all of the business, undertaking or assets of a Subsidiary Undertaking which immediately prior to such transfer is a Principal Subsidiary, whereupon the transferor Subsidiary Undertaking shall immediately cease to be a Principal Subsidiary and the transferee Subsidiary Undertaking shall become a Principal Subsidiary until publication of its next audited accounts when whether or not it shall continue to be a Principal Subsidiary shall be determined pursuant to sub-paragraph (a). A certificate signed by two directors for the time being of the Guarantor that in their opinion a Subsidiary Undertaking is not or was or was not at any particular time a Principal Subsidiary shall, in the absence of manifest error, be conclusive and binding on all parties. Additionally, Reiver Holdings Limited, Reiver Finance Limited, Bakethin Holdings Limited and Bakethin Finance PLC shall not be Principal Subsidiaries notwithstanding that they may otherwise have been by virtue of the other provisions of this paragraph.

**“Subsidiary Undertaking”** means, in relation to any entity, a subsidiary undertaking of such entity within the meaning of Section 1162 of the Companies Act 2006.

**“Threshold Amount”** means the higher of (a) £15,000,000 (or its equivalent in any other currency or currencies on the relevant date as determined by the Trustee) and (b) 2 per cent. of Net Tangible Assets of the Guarantor.

## **9 Enforcement**

At any time after the Bonds become due and payable, the Trustee may, at its discretion and without further notice, institute such proceedings and/or steps and/or actions against the Issuer and/or the Guarantor as it may think fit to enforce the obligations of the Issuer and/or the Guarantor under the Bonds, the Coupons or the Trust Deed, but it shall not be bound to take any such proceedings and/or steps and/or actions unless (i) it shall have been so directed by an Extraordinary Resolution or so requested in writing by the holders of at least one quarter in principal amount of the Bonds then outstanding and (ii) it shall have been indemnified and/or secured and/or pre-funded to its satisfaction. No Bondholder or Couponholder may proceed directly against the Issuer or the Guarantor unless the Trustee, having become bound to proceed, fails to do so and such failure is continuing.

## **10 Replacement of Bonds and Coupons**

Should any Bond or Coupon be lost, stolen, mutilated, defaced or destroyed it may be replaced at the specified office of the Principal Paying Agent upon payment by the claimant of the expenses incurred in connection with such replacement and on such terms as to evidence and indemnity as the Issuer may require (provided that the requirement is reasonable in the light of prevailing market practice). Mutilated or defaced Bonds or Coupons must be surrendered before replacements will be issued.

## **11 Notices**

All Notices to Bondholders shall be deemed to have been duly given if published in a leading daily newspaper of general circulation in the United Kingdom (expected to be the Financial Times) or, if this is not possible, in another leading English language newspaper having general circulation in Europe previously approved by the Trustee. Any such notice shall be deemed to have been given on the date of such publication or, if published more than once, on the first date on which publication is made. If publication as provided above is not practicable, notice will be given in such other manner, and shall be deemed to have been given on such date, as the Trustee may approve.

Couponholders will be deemed for all purposes to have notice of the contents of any notice given to the Bondholders in accordance with this Condition.

## **12 Meetings of Bondholders; Modifications; Waiver; Substitution**



The Trust Deed contains provisions for convening meetings of the Bondholders to consider any matter affecting their interests, including proposals to modify by Extraordinary Resolution these Conditions or the provisions of the Trust Deed. The quorum at any such meeting for passing an Extraordinary Resolution will be two or more persons holding or representing a majority in outstanding principal amount of the Bonds for the time being outstanding or, at any adjourned meeting, two or more persons being or representing Bondholders whatever the outstanding principal amount of the Bonds so held or represented, except that, at any meeting the business of which includes the modification of certain material terms and conditions of the Bonds and provisions of the Trust Deed (as set out therein, including the maturity date of the Bonds and the dates for payments of interest thereon, the status of the Bonds, the outstanding principal amount of, and interest payable on, the Bonds, the currency of the Bonds, the Guarantee and the quorum requirements for meetings of Bondholders), the necessary quorum for passing an Extraordinary Resolution will be two or more persons holding or representing not less than three-quarters, or at any such adjourned meeting not less than one-quarter, of the outstanding principal amount of the Bonds for the time being outstanding. An Extraordinary Resolution passed at any meeting of Bondholders will be binding on all Bondholders, whether or not they are present at the meeting, and on all Couponholders.

The Trustee may agree, without the consent of the Bondholders or Couponholders, to any modification of (except as mentioned in the Trust Deed), or to any waiver or authorisation of any breach or proposed breach of, any of these Conditions or any provision of the Trust Deed which, in the opinion of the Trustee, is not materially prejudicial to the interests of the Bondholders, or to any modification which is in its opinion of a formal, minor or technical nature or made to correct a manifest error.

Any such modification, waiver or authorisation shall be binding on the Bondholders and the Couponholders and, unless the Trustee agrees otherwise, any such modification shall be notified to the Bondholders as soon as practicable thereafter.

The Trust Deed provides that a resolution in writing signed by or on behalf of the holders of not less than 90 per cent. in principal amount of the Bonds for the time being outstanding shall for all purposes be as valid and effective as an Extraordinary Resolution passed at a meeting of Bondholders duly convened and held. 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.

The Trustee may agree to the substitution at any time or times of any successor company (as defined in the Trust Deed) of the Issuer or any Subsidiary or any holding company (as defined in the Trust Deed) of the Issuer or the Guarantor or any successor company of the Guarantor, as the principal debtor under the Trust Deed and the Bonds. Such agreement shall also be subject to the relevant provisions of the Trust Deed, including (other than where the substitute obligor is the Guarantor or any successor company of the Guarantor) the irrevocable and unconditional guarantee in respect of the Bonds by the Guarantor. In the case of any proposed substitution, the Trustee may agree without the consent of the Bondholders or the Couponholders, to a change of the law governing the Bonds, the Coupons and/or the Trust Deed provided that such change would not, in the opinion of the Trustee, be materially prejudicial to the interests of the Bondholders.

In connection with the exercise of its powers, trusts, authorities and discretions (including, but not limited to, those in relation to any proposed substitution or change of law as aforesaid), the Trustee shall not have regard to the consequences and, in particular, the tax consequences of such exercise for individual Bondholders or Couponholders resulting from their being for any purpose domiciled or resident in, or otherwise connected with, or subject to the jurisdiction of, any particular territory, and the Trustee shall not be entitled to require, nor shall any Bondholder or Couponholder be entitled to claim, from the Issuer or the Guarantor any indemnification or payment in respect of any tax consequence of any such exercise upon individual Bondholders or Couponholders.

### **13 Indemnification of the Trustee**

The Trust Deed contains provisions for the indemnification of the Trustee and for its relief from responsibility, including provisions relieving it from taking proceedings and/or any steps and/or actions to enforce repayment unless indemnified and/or secured and/or pre-funded to its satisfaction. The Trustee will be entitled to enter into business transactions with the Issuer or the Guarantor or any Subsidiary Undertaking (as defined in Condition 8) of the Issuer or the Guarantor without accounting for any profits resulting from any such transactions. The Issuer, the Paying Agents and

the Trustee, as appropriate, shall have no responsibility for errors or omissions in any calculations and determinations made hereunder and all such calculations and determinations (save in the case of manifest error) shall be final and binding on the Issuer, the Guarantor, the Paying Agents and the Bondholders.

The Trustee is entitled to rely on any report or certificate of the Issuer, the Guarantor, directors of the Issuer or the Guarantor, any Independent Financial Adviser, auditors, broker or other experts whether or not their liability in relation thereto is limited (by reference to a monetary cap or otherwise).

#### **14 Further Issues**

The Issuer may from time to time without the consent of the Bondholders create and issue further bonds, notes or debentures (whether in bearer or registered form) either having the same terms and conditions as the Bonds in all respects (or in all respects except for the first payment of interest on them) and so that such further issue shall be consolidated and form a single series with the outstanding Bonds, or upon such terms as to interest, conversion, premium, redemption and otherwise as the Issuer may determine at the time of their issue. Any such further bonds, notes or debentures forming a single series with the outstanding bonds, notes or debentures of any series (including the Bonds) constituted by the Trust Deed or any deed supplemental to it shall, and any other bonds, notes or debentures may, with the consent of the Trustee, be constituted by a deed supplemental to the Trust Deed. The Trust Deed contains provisions for convening a single meeting of the Bondholders and the holders of bearer or registered bonds, notes or debentures of other series in certain circumstances where the Trustee so decides.

#### **15 Prescription**

Bonds will become void unless presented for payment within 10 years and (subject to Condition 6) Coupons within 5 years from their respective Relevant Dates.

#### **16 Governing Law**

The Bonds, the Coupons and the Trust Deed, and any non-contractual obligations arising out of or in connection with the Bonds, the Coupons and the Trust Deed, are governed by and shall be construed in accordance with English law.

#### **17 Contracts (Rights of Third Parties) Act 1999**

No person shall have any right to enforce any provision of these Conditions under the Contracts (Rights of Third Parties) Act 1999.

## Summary of Provisions relating to the Bonds while in Global Form

The Temporary Global Bond and the Permanent Global Bond contain provisions which apply to the Bonds while they are in global form, some of which modify the effect of the terms and conditions of the Bonds set out in this Prospectus. The following is a summary of certain of those provisions:

### 1 Exchange

The Temporary Global Bond is exchangeable in whole or in part for interests in the Permanent Global Bond on or after a date which is expected to be 21 November 2016 upon certification as to non-U.S. beneficial ownership in the form set out in the Temporary Global Bond. The Permanent Global Bond is exchangeable in whole but not in part (free of charge to the holder) for the definitive Bonds described below (1) if the Permanent Global Bond is held on behalf of a clearing system and such clearing system is closed for business for a continuous period of 14 days (other than by reason of holidays, statutory or otherwise) or announces an intention permanently to cease business or does in fact do so, (2) if the Issuer would suffer a material disadvantage in respect of the Bonds as a result of a change in the laws or regulations (taxation or otherwise) of any jurisdiction referred to in Condition 7 or as a result of a change in the practice of any clearing system which would not be suffered were the Bonds in definitive form and a certificate to such effect signed by two directors of the Issuer is delivered to the Trustee. Thereupon (in the case of (1) above) the holder of the Permanent Global Bond (acting on the instructions of one more of entitled accountholders) or the Trustee may give notice to the Principal Paying Agent, and (in the case of (2) above) the Issuer may give notice to the Trustee and the Bondholders, of its intention to exchange the Permanent Global Bond for definitive Bonds on or after the Exchange Date (as defined below) specified in the notice.

On or after the Exchange Date the holder of the Permanent Global Bond may (in the case of (1) above) and shall (in the case of (2) above) surrender the Permanent Global Bond to or to the order of the Principal Paying Agent. In exchange for the Permanent Global Bond, the Issuer will deliver, or procure the delivery of, an equal aggregate outstanding principal amount of duly executed and authenticated definitive Bonds (having attached to them all Coupons in respect of interest which has not already been paid on the Permanent Global Bond), security printed in accordance with any applicable legal and stock exchange requirements and in or substantially in the form set out in Schedule 1 to the Trust Deed. On exchange of the Permanent Global Bond, the Issuer will, if the holder so requests, procure that it is cancelled and returned to the holder together with any relevant definitive Bonds.

“**Exchange Date**” means a day falling not less than 60 days after that on which the notice requiring exchange is given and on which banks are open for business in the city in which the specified office of the Principal Paying Agent is located and, except in the case of exchange pursuant to (1) above, in the city in which the relevant clearing system is located.

### 2 Payments

No payment will be made on the Temporary Global Bond unless exchange for an interest in the Permanent Global Bond is improperly withheld or refused. Payments of principal, any premium and interest in respect of Bonds represented by the Permanent Global Bond will be made against presentation for endorsement and, if no further payment falls to be made in respect of the Bonds, surrender of the Permanent Global Bond to or to the order of the Principal Paying Agent or such other Paying Agent as shall have been notified to the Bondholders for such purpose. A record of each payment so made will be endorsed in the appropriate schedule to the Permanent Global Bond, which endorsement will be *prima facie* evidence that such payment has been made in respect of the Bonds. For the purpose of any payments made in respect of the Permanent Global Bond, references to Bonds or Coupons being “presented for payment” in Condition 6 shall not apply, and all such payments shall be made on a day on which commercial banks and foreign exchange markets are open for business in London.

### 3 Notices

So long as the Bonds are represented by the Permanent Global Bond and the Permanent Global Bond is held on behalf of a clearing system, notices to Bondholders may be given by delivery of the relevant notice to that clearing system for communication by it to entitled accountholders in substitution for publication as required by the Conditions. Any such notice (if not also published in

accordance with Condition 11) shall be deemed to have been given to Bondholders on the second day after the day on which such notice is delivered to the clearing system(s) as aforesaid.

#### **4 Prescription**

Claims against the Issuer and the Guarantor in respect of principal, any premium and interest on the Bonds while the Bonds are represented by the Permanent Global Bond will become void unless it is presented for payment within a period of 10 years (in the case of principal and any premium) and five years (in the case of interest) from the appropriate Relevant Date (as defined in Condition 7).

#### **5 Meetings**

The holder of the Permanent Global Bond will be treated as being two persons for the purposes of any quorum requirements of a meeting of Bondholders and, at any such meeting, as having one vote in respect of each £1,000 in outstanding principal amount of Bonds for which the Permanent Global Bond may be exchanged.

#### **6 Purchase and Cancellation**

Cancellation of any Bond required by the Conditions to be cancelled following its redemption or purchase will be effected by reduction in the outstanding notional amount of the Permanent Global Bond.

#### **7 Trustee's Powers**

In considering the interests of Bondholders while the Permanent Global Bond is held on behalf of a clearing system the Trustee may have regard to any information provided to it by such clearing system or its operator as to the identity (either individually or by category) of its accountholders with entitlements to the Permanent Global Bond and may consider such interests as if such accountholders were the holder of the Permanent Global Bond.

#### **8 Put Option**

The Bondholders' put option in Condition 5(d) may be exercised by the holder of the Permanent Global Bond giving notice to the Principal Paying Agent of the outstanding principal amount of Bonds in respect of which the option is exercised and presenting the Permanent Global Bond for endorsement of exercise within the time limits specified in Condition 5(d).

#### **9 Electronic Consent and Written Resolution**

While any Temporary or Permanent Global Bond is held on behalf of a relevant clearing system, then:

- (a) approval of a resolution proposed by the Issuer or the Trustee (as the case may be) given by way of electronic consents communicated through the electronic communications systems of the relevant clearing system(s) in accordance with their operating rules and procedures by or on behalf of the holders of not less than 75 per cent. in principal amount of the Bonds outstanding (an "**Electronic Consent**" as defined in the Trust Deed) shall, for all purposes (including matters that would otherwise require an Extraordinary Resolution to be passed at a meeting for which a special quorum resolution (as defined in the Trust Deed) is required), take effect as an Extraordinary Resolution passed at a meeting of Bondholders duly convened and held, and shall be binding on all Bondholders and holders of Coupons whether or not they participated in such Electronic Consent; and
- (b) where Electronic Consent is not being sought, for the purpose of determining whether a Written Resolution (as defined in the Trust Deed) has been validly passed, the Issuer and the Trustee shall be entitled to rely on consent or instructions given in writing directly to the Issuer and/or the Trustee, as the case may be, by (a) accountholders in the clearing system with entitlements to such Global Bond and/or, (b) where the accountholders hold any such entitlement on behalf of another person, on written consent from or written instruction by the person identified by that accountholder as the person for whom such entitlement is held. For the purpose of establishing the entitlement to give any such consent or instruction, the Issuer

and the Trustee shall be entitled to rely on any certificate or other document issued by, in the case of (a) above, Euroclear, Clearstream, Luxembourg or any other relevant alternative clearing system and, in the case of (b) above, the relevant alternative clearing system and the accountholder identified by such relevant alternative clearing system for the purposes of (b) above. Any resolution passed in such manner shall be binding on all Bondholders and Couponholders, even if the relevant consent or instruction proves to be defective. Any such certificate or other document may comprise any form of statement or print out of electronic records provided by the relevant clearing system (including Euroclear's EUCLID or Clearstream, Luxembourg's CreationOnline system) in accordance with its usual procedures and in which the accountholder of a particular principal or nominal amount of the Bonds is clearly identified together with the amount of such holding. Neither the Issuer, the Guarantor nor the Trustee shall be liable to any person by reason of having accepted as valid or not having rejected any certificate or other document to such effect purporting to be issued by any such person and subsequently found to be forged or not authentic.

### **Use of Proceeds**

The net proceeds of the issue are estimated to amount to £298,242,000, which are expected to be used in part to refinance certain of the Issuer's existing indebtedness and any remainder for general corporate purposes.

## Northumbrian Water Finance Plc

### Information about the Issuer

The legal and commercial name of the Issuer is Northumbrian Water Finance Plc.

The Issuer is a public limited company registered in England and Wales with registered number 4326507 and was incorporated on 21 November 2001. The Issuer operates under the Companies Act 2006.

The registered office of the Issuer is Northumbria House, Abbey Road, Pity Me, Durham DH1 5FJ, United Kingdom and its telephone number is +44 (0)870 608 4820.

### Business Overview

The Issuer is a finance vehicle. The principal activity of the Issuer is to raise finance on behalf of the Guarantor.

### Organisational Structure

The Issuer is part of the Group and is a subsidiary of the Guarantor. See “Northumbrian Water Limited – Organisational Structure” below.

The Issuer has no subsidiaries.

The Issuer is dependent on the Guarantor to meet its cashflow requirements. The sole function of the Issuer is to raise finance for the Guarantor, and funds raised by it are on-lent to the Guarantor. The Issuer is reliant on receiving funds from the Guarantor, *inter alia*, to enable it to service the interest and principal payments in respect of its finance obligations.

### Administrative, Management and Supervisory Bodies

The Directors of the Issuer (each of whom is an executive director) and their respective roles as directors of the Guarantor are as follows:

<i>Name</i>	<i>Role as director of the Guarantor</i>
Heidi Mottram	Chief Executive Officer of the Guarantor
Christopher Ian Johns	Finance Director of the Guarantor

There are no potential conflicts of interest between the Directors and their private interests or their other duties.

The Company Secretary of the Issuer is Martin Parker.

The business address of each of the above is Northumbria House, Abbey Road, Pity Me, Durham DH1 5FJ, United Kingdom.

### Major Shareholders

The authorised and issued share capital of the Issuer is £50,000 comprising 50,000 ordinary shares of £1 each of which 49,999 are held by the Guarantor and one is held by Martin Parker on trust for the Guarantor. As at the date of this Prospectus, 75p per share remains unpaid.

There are no arrangements in place the operation of which may result in a change of control of the Issuer.

## Northumbrian Water Limited

### Information about the Guarantor

The legal name of the Guarantor is Northumbrian Water Limited and it trades commercially in the north east of England (the “**NE Region**”) as “Northumbrian Water”, and in the south east of England (the “**SE Region**”) as “Essex and Suffolk Water”.

The Guarantor is a private limited company registered in England and Wales with registered number 02366703 and was incorporated on 1 April 1989. The Guarantor operates under the Companies Act 2006.

The registered office of the Guarantor is Northumbria House, Abbey Road, Pity Me, Durham DH1 5FJ, United Kingdom and its telephone number is +44 (0)870 608 4820.

### Business Overview

The Guarantor is engaged in the provision of water and sewerage services in the NE Region and water only services in the SE Region under an appointment (as varied from time to time, the “**Appointment**”) granted by the Secretary of the State pursuant to the Water Act 1989 (now, the Water Industry Act 1991) and as such it operates a “regulated business”.

In the NE Region, the Guarantor operates in a geographical area of approximately 9,400 square kilometres, which has an estimated total resident population of approximately 2.7 million. The largest centres of population are concentrated along the coasts of south Northumbria, Tyne and Wear, County Durham and Cleveland and, in particular, around the estuaries of the River Tyne, Wear and Tees.

In the SE Region, the Guarantor operates in a geographical area of approximately 2,850 square kilometres and has an estimated total resident population of approximately 1.8 million. The largest centres of population are concentrated along the coasts of Norfolk, Suffolk and Essex and, in particular, around the estuary of the River Thames and the towns of Great Yarmouth, Lowestoft and Chelmsford.

The Guarantor supplies water and sewerage services to approximately 1.2 million properties in the NE Region and water services to approximately 0.8 million properties in the SE Region. Significant quantities of metered and partially treated water are supplied to twelve industrial customers on Teesside in the NE Region.

For the financial year ended 31 March 2016, the turnover of the Guarantor was £805.5 million.

During 2014, OFWAT concluded its periodic price review for AMP6, which runs from April 2015 to March 2020 (“**PR14**”). As part of its periodic AMP reviews, OFWAT sets the prices a water company can charge its customers which are intended to allow the companies to finance their operations and earn a reasonable return on capital. As part of the AMP6 process, OFWAT has set separate, binding revenue caps for water wholesale and wastewater wholesale activities, with an inflation adjustment. OFWAT has also set controls for the pricing of household retail activities (based on an “average cost to serve”) and non-household retail activities (where “default tariffs” are set to protect customers who do not or are not able to switch).

The water resources of the NE Region are more than twice present supply requirements. Approximately 90 per cent. of all water supplied in the SE Region emanates from surface water sources, with the majority of the remaining demand coming from underground sources in the south Suffolk area. The capacity of Abberton reservoir, a major water resource in the SE region, was increased by approximately 60 per cent. Overall, the average demand for water is close to the reliable yield and the Guarantor believes it is operating the most economic blend of demand management and additional resource development to ensure reliability of supply in future years.

### Organisational Structure

The Guarantor is a wholly owned subsidiary of Northumbrian Water Group Limited (“**NWGL**”).

On 14 October 2011 a consortium of Cheung Kong Infrastructure Holdings Limited, Cheung Kong (Holdings) Limited and Li Ka Shing Foundation Limited, through UK Water (2011) Limited (“**UKW**”), acquired, by way of a scheme of arrangement, the entire share capital of Northumbrian Water Group plc (formerly Aquavit plc) (“**NWG**”) for a cash consideration of £2.4 billion. In connection with such acquisition, UK Water (2011) Limited raised £232 million of bank debt, which was subsequently pushed down to the Guarantor in November 2011. Following the acquisition, NWG changed its status to a private limited company from a public limited company and became, what is now, NWGL.

On 8 March 2013, UKW undertook a restructuring to simplify the group structure which included the distribution of its 100 per cent. shareholding in NWGL to its shareholders and the novation to NWGL of

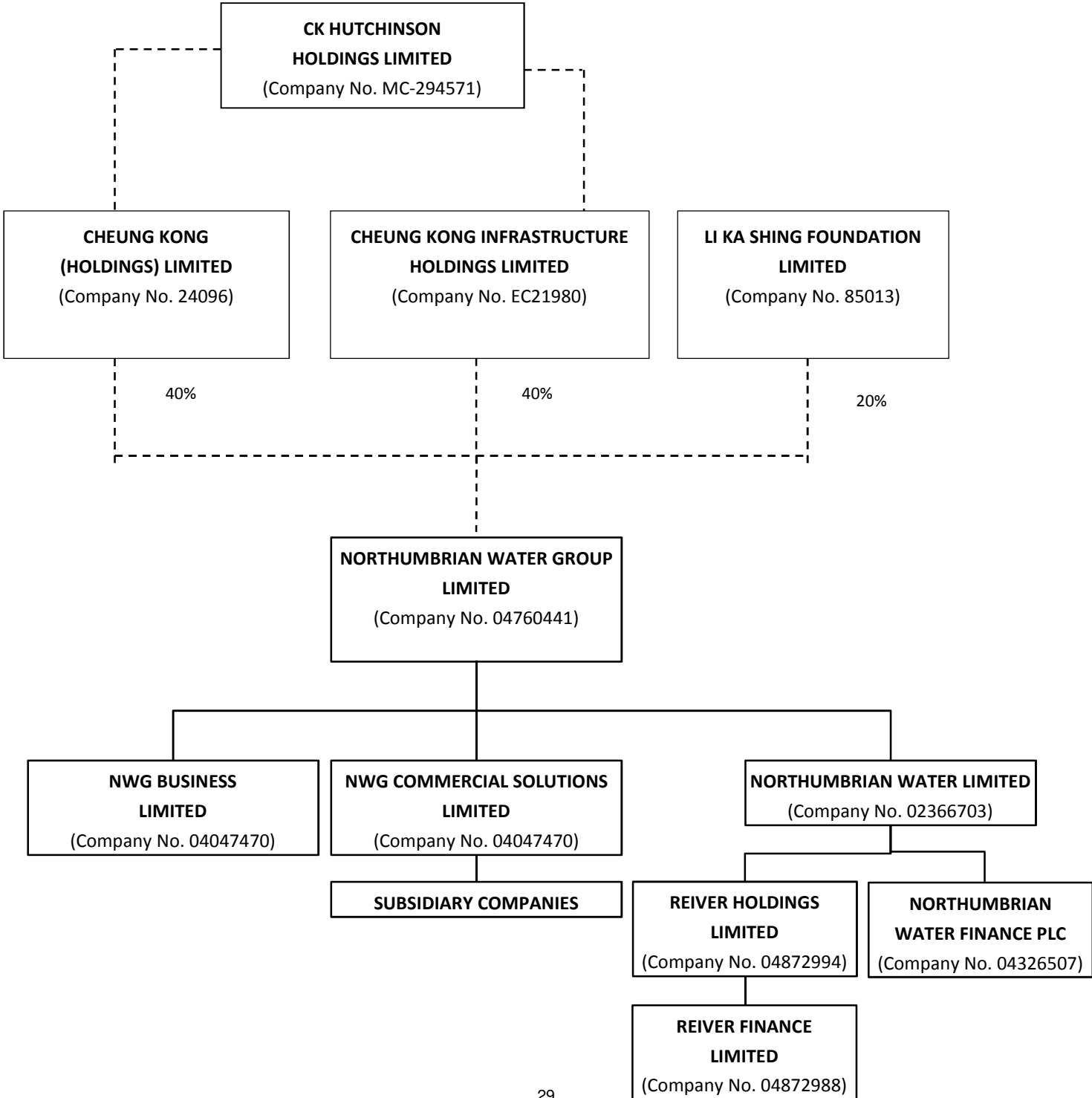


UKW's shareholder loan notes and interest outstanding for consideration left outstanding. As a result, UKW is in the process of being wound up. This consideration was ultimately settled by way of offset against a dividend declared by NWGL. On the same date, Northumbrian Services Limited (“NSL”) and the Guarantor became directly wholly owned subsidiaries of NWGL and NWG also undertook a reorganisation of its ordinary share capital. Also during the course of 2013, Atlantic Water Limited was wound up.

In 2016 and in line with the Group’s strategy to rationalise the Group’s consolidated balance sheet, the Group disposed of the entire share capital of NSL by way of a dividend in specie.

The Guarantor has three subsidiaries and two quasi-subsidiary special purpose entities, Bakethin Holdings Limited which is wholly owned by Bakethin Charitable Trust and Bakethin Finance plc which is a wholly owned subsidiary of Bakethin Holdings Limited. The principal activity of Bakethin Finance plc is as a special purpose financing vehicle.

The structure of the Group and its ownership structure is as shown below:



## **Administrative, Management and Supervisory Bodies**

The Board of Directors of the Guarantor and their business addresses are as follows:

<i>Name</i>	<i>Title</i>	<i>Business Address</i>
Andrew John Hunter	Non-Executive Chairman	<i>Cheung Kong Infrastructure Holdings, 12th Floor, Cheung Kong Center, 2 Queen's Road Central, Hong Kong</i>
Heidi Mottram	Chief Executive Officer	<i>Northumbria House, Abbey Road Pity Me, Durham, DH1 5FJ</i>
Christopher Johns	Director	<i>Northumbria House, Abbey Road Pity Me, Durham, DH1 5FJ</i>
Ceri Jones	Assets and Assurance Director	<i>Northumbria House, Abbey Road Pity Me, Durham, DH1 5FJ</i>
Frank Frame	Non-Executive Director	<i>Northumbria House, Abbey Road Pity Me, Durham, DH1 5FJ</i>
Dr Simon Lyster	Independent Non-Executive Director	<i>Northumbria House, Abbey Road Pity Me, Durham, DH1 5FJ</i>
Margaret Fay	Independent Non-Executive Director	<i>Northumbria House, Abbey Road Pity Me, Durham, DH1 5FJ</i>
Paul Rew	Senior Independent Non-Executive Director	<i>Northumbria House, Abbey Road Pity Me, Durham, DH1 5FJ</i>
Martin Nègre	Independent Non-Executive Director	<i>Northumbria House, Abbey Road Pity Me, Durham, DH1 5FJ</i>
Duncan Macrae	Non-Executive Director	<i>Cheung Kong Infrastructure Holdings, 12th Floor, Cheung Kong Center, 2 Queen's Road Central, Hong Kong</i>
Hing Lam Kam	Non-Executive Director	<i>Cheung Kong (Holdings) Limited, 7th Floor, Cheung Kong Center, 2 Queen's Road Central, Hong Kong</i>
Loi Shun Chan	Alternative Non-Executive Director	<i>Cheung Kong (Holdings) Limited, 7th Floor, Cheung Kong Center, 2 Queen's Road Central, Hong Kong</i>
Wai Che Wendy Tong Barnes	Alternative Non-Executive Director	<i>Northumbria House, Abbey Road Pity Me, Durham, DH1 5FJ</i>

In accordance with the terms of the Appointment, the Guarantor is required to have at least three independent Non-Executive Directors. As at the date of this Prospectus, those Directors are Paul Rew, Dr Simon Lyster, Martin Nègre and Margaret Fay.

There are no potential conflicts of interest between the Directors and their private interests or their other duties.

The Company Secretary of the Guarantor is Martin Parker.

The business address of each of the above is Northumbria House, Abbey Road, Pity Me, Durham DH1 5FJ, United Kingdom (the registered and head office of the Guarantor).

## Taxation

The comments below are of a general nature based on current United Kingdom tax law, as applied in England and Wales, and H.M. Revenue and Customs (“HMRC”) practice (which may not be binding on HMRC). They do not necessarily apply where the income is deemed for tax purposes to be the income of any other person. They relate only to the position of persons who hold the Bonds and Coupons as investments and are the absolute beneficial owners of their Bonds and Coupons. They may not apply to certain classes of person such as dealers or certain professional investors. Any Bondholders who may be subject to tax in a jurisdiction other than the United Kingdom or who are in doubt as to their own tax position should consult their professional advisers.

### Interest

While the Bonds continue to be listed on a recognised stock exchange within the meaning of section 1005 of the Income Tax Act 2007, payments of interest may be made without withholding or deduction for or on account of United Kingdom income tax. The London Stock Exchange is a recognised stock exchange for these purposes. Under HMRC published practice, securities will be treated as listed on the London Stock Exchange if they are admitted to the Official List (within the meaning of and in accordance with the provisions of the Financial Services and Markets Act 2000) by the United Kingdom Listing Authority and are admitted to trading on the London Stock Exchange. Provided, therefore, that the Bonds become and remain so listed, interest on the Bonds will be payable by the Issuer without withholding or deduction on account of United Kingdom tax.

If the Bonds cease to be listed, interest will generally be paid by the Issuer under deduction of income tax at the basic rate (currently 20 per cent.) unless (i) at the time the payment is made, the Issuer reasonably believes that the person beneficially entitled to the interest is:

- a) a company resident in the United Kingdom; or
- b) a company not resident in the United Kingdom which carries on a trade in the United Kingdom through a permanent establishment and which brings into account the interest in computing its United Kingdom taxable profits; or
- c) a partnership each member of which is a company referred to in (a) or (b) above or a combination of companies referred to in (a) or (b) above,

in each case provided that HMRC has not given a direction (in circumstances where it has reasonable grounds to believe that it is likely that the above exemption is not available in respect of such payment of interest at the time the payment is made) that the interest should be paid under deduction of tax or (ii) the Issuer has received direction to the contrary from HMRC in respect of such relief as may be available pursuant to the provisions of any applicable double taxation treaty or (iii) any other relief applies.

The interest has a United Kingdom source and accordingly may be chargeable to United Kingdom tax by direct assessment. Where the interest is paid without withholding or deduction on account of United Kingdom tax, the interest will not be assessed to United Kingdom tax in the hands of holders of the Bonds (other than certain trustees) who are not resident for tax purposes in the United Kingdom, except where such persons carry on a trade, profession or vocation in the United Kingdom through a United Kingdom branch or agency or, in the case of a corporate holder, carries on a trade through a permanent establishment in the United Kingdom in connection with which the interest is received or to which the Bonds are attributable, in which case (subject to exemptions for interest received by certain categories of agent, such as some brokers and investment managers) tax may be levied on the United Kingdom branch, agency or permanent establishment.

If interest were paid under deduction of United Kingdom income tax (e.g. if the Bonds lost their listing), 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 an applicable double taxation treaty.

Bondholders should note that the provisions relating to additional amounts referred to in the section entitled “Terms and Conditions of the Bonds – Taxation” would not apply if HMRC sought to assess directly the person entitled to the relevant interest to United Kingdom tax. However exemption from, or reduction of, such United Kingdom tax liability might be available under an applicable double taxation treaty.

The United Kingdom withholding tax treatment of payments by the Guarantor under the terms of the Guarantee in respect of interest on the Bonds is uncertain. Accordingly, if the Guarantor makes any payments in respect of interest on the Bonds (or other amounts due under the Bonds other than the

repayment of amounts subscribed for the Bonds), such payments may be subject to withholding on account, of United Kingdom income tax at the basic rate (currently 20 per cent.), subject to the availability of other reliefs or to any direction to the contrary from HMRC in respect of such relief as may be available pursuant to the provisions of any applicable double taxation treaty.

### **Corporate Bondholders**

Bondholders within the charge to United Kingdom corporation tax (including non-resident Bondholders whose Bonds are used, held or acquired for the purposes of a trade carried on in the United Kingdom through a permanent establishment) will normally be required to recognise any profits, gains or losses on the Bonds (including on redemption) for United Kingdom corporation tax purposes under the “loan relationship” rules in Part 5 of the Corporation Tax Act 2009. Such Bondholders will generally be charged in each accounting period by reference to interest and other amounts which, in accordance with generally accepted accounting practice, are recognised in determining the Bondholder’s profit or loss for that period. Fluctuations in value relating to foreign exchange gains and losses in respect of the Bonds will be brought into account as income.

### **Other Bondholders**

Bondholders who are either individuals or trustees and are resident for tax purposes in the United Kingdom or who carry on a trade, profession or vocation in the United Kingdom through a branch or agency to which the Bonds are attributable will generally be liable to United Kingdom tax on the amount of any interest received in respect of the Bonds.

The Bonds are “qualifying corporate bonds” within the meaning of section 117 of the Taxation of Chargeable Gains Act 1992 with the result that on a disposal of the Bonds neither chargeable gains nor allowable losses will arise for the purposes of taxation of capital gains.

On a disposal of the Bonds by a Bondholder, an amount representing any interest which has accrued since the last interest payment date may be chargeable to tax as income under the rules of the accrued income scheme as set out in Part 12 of the Income Tax Act 2007, if that Bondholder is either an individual or a trustee and is resident in the United Kingdom or carries on a trade, profession or vocation in the United Kingdom through a branch or agency to which the Bonds are attributable.

### **United Kingdom Stamp Duty and Stamp Duty Reserve Tax**

No United Kingdom Stamp Duty or Stamp Duty Reserve Tax is payable on the issue or transfer by delivery of a Bond or on its redemption.

### **US Foreign Account Tax Compliance Act (“FATCA”) and other exchange of information requirements**

The US-UK Agreement to Improve International Tax Compliance and to Implement FATCA (the “**US-UK IGA**”) was entered into with the intention of enabling the UK implementation of the FATCA provisions of the U.S. Hiring Incentives to Restore Employment Act, which impose a reporting regime and potentially a 30 per cent. withholding tax on certain payments made from (or attributable to) US sources or in respect of US assets to certain categories of recipient including a non-US financial institution (a “**foreign financial institution**” or “**FFI**”) that does not comply with the terms of FATCA and is not otherwise exempt. Certain financial institutions (“**reporting financial institutions**”) are required to provide certain information about their US accountholders to HMRC (which information will in turn be provided to the US tax authorities) pursuant to UK regulations implementing the FACTA. It is not expected that the Issuer will constitute an FFI for this purpose. However, if the Issuer qualified as an FFI, the Issuer would be required to provide certain information about its Bondholders to HMRC (which information will in turn be provided to the US tax authorities) and would also be required to register with the US tax authorities. In the event that the Issuer is registered and does not comply with FACTA, a 30 per cent. withholding tax may be imposed on payments it receives from (or which are attributable to) US sources or in respect of US assets, which may reduce the amounts available to it to make payments to the Bondholders.

A number of jurisdictions, including the UK, have implemented and entered into multilateral arrangements modelled on the Common Reporting Standard (“**CRS**”) for Automatic Exchange of Financial Account Information published by the Organisation for Economic Co-operation and Development (“**OECD**”). It is not expected that the Issuer will constitute a financial institution (“**FI**”) for this purpose. However, if the Issuer qualified as an FI, it would be required to provide certain information to HMRC about Bondholders that are resident in the jurisdictions which are party to such arrangements (which information would in turn be provided to the relevant tax authorities). In light of the above, Bondholders may be required to provide certain information to the Issuer to enable the Issuer to comply with the terms of the UK regulations.

FATCA AND CRS ARE PARTICULARLY COMPLEX AND THEIR APPLICATION TO THE ISSUER IS UNCERTAIN AT THIS TIME. EACH HOLDER OF BONDS SHOULD CONSULT ITS OWN TAX ADVISER TO OBTAIN A MORE DETAILED EXPLANATION OF FATCA AND CRS AND TO DETERMINE HOW THIS LEGISLATION MIGHT AFFECT EACH HOLDER IN ITS PARTICULAR CIRCUMSTANCES.

## Subscription and Sale

The Managers have, pursuant to a Subscription Agreement (the “**Subscription Agreement**”) dated 7 October 2016, agreed with the Issuer and the Guarantor to subscribe and pay for the Bonds at the issue price of 99.764 per cent. of the principal amount of the Bonds. The Managers are entitled to terminate the Subscription Agreement in certain circumstances prior to any payment for the Bonds being made to the Issuer. The Issuer and the Guarantor have agreed to indemnify the Managers against certain liabilities in connection with the issue of the Bonds.

The Bonds have not been and will not be registered under the Securities Act, and may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons except in certain transactions exempt from the registration requirements of the Securities Act. Terms used in this paragraph have the meanings given to them by Regulation S under the Securities Act.

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

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

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

Each Manager has represented and agreed that (i) it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to the Bonds in, from or otherwise involving the United Kingdom; and (ii) 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 the FSMA does not apply to the Issuer or the Guarantor.

No action has been taken by the Issuer, the Guarantor or the Managers that would, or is intended to, permit a public offer of the Bonds in any country or jurisdiction where any such action for that purpose is required. Accordingly, each of the Managers has represented and agreed that (a) it will comply (to the best of its knowledge and belief) with all applicable laws and regulations in each jurisdiction in which it acquires offers, sells or delivers Bonds or has in its possession or distributes this Prospectus or any amendment or supplement to it or any other offering material and (b) it will obtain any consent, approval or permission required by it for the acquisition, offer, sale or delivery by it of the Bonds under the laws and regulations in force in any jurisdiction to which it is subject or from which it makes any acquisition, offer, sale or delivery.

## General Information

1. The Bonds have been accepted for clearance through Clearstream, Luxembourg and Euroclear. The Common Code reference number for the Bonds is 149972463 and the International Security Identification Number for the Bonds is XS1499724638. The address of Euroclear is Euroclear Bank S.A./N.V. , 1 Boulevard du Roi Albert II, B-1210 Brussels, Belgium and the address of Clearstream, Luxembourg is Clearstream Banking S.A., 42 Avenue JF Kennedy, L-1855 Luxembourg.

2. The listing of the Bonds on the Official List will be expressed as a percentage of their principal amount (exclusive of accrued interest). It is expected that listing of the Bonds on the Official List and admission of the Bonds to trading on the Market will be granted on or around 11 October 2016 subject only to the issue of the Temporary Global Bond. Prior to official listing and admission to trading, however, dealings will be permitted by the London Stock Exchange in accordance with its rules. It is current market practice that any transactions will normally be effected for settlement in Sterling and for delivery on the third working day after the day of the transaction. The total expenses relating to the admission to trading of the Bonds are expected to be approximately £6,200.

3. The Issuer and the Guarantor have obtained all necessary consents, approvals and authorisations in the United Kingdom in connection with the issue of the Bonds and the giving of the Guarantee, respectively. The issue of the Bonds was authorised pursuant to a resolution of the Board of Directors of the Issuer passed on 28 September 2016 and the giving of the Guarantee by the Guarantor was authorised pursuant to a resolution passed on 28 September 2016 of the Standing Committee of the Board of Directors of the Guarantor established during April 2000 and ratified pursuant to a resolution of the Board of Directors of the Guarantor passed on 31 March 2011.

4. There has been (i) no significant change in the financial or trading position of the Issuer since 31 March 2016 and no material adverse change in the prospects of the Issuer since 31 March 2016 and (ii) no significant change in the financial or trading position of the Guarantor and the Group since 31 March 2016 and no material adverse change in the prospects of the Guarantor and the Group since 31 March 2016.

5. There are no, nor have there been during the 12 months preceding the date of this Prospectus, any governmental, legal or arbitration proceedings which may have, or have had significant effects on the financial position or profitability of the Issuer, the Group or of the Guarantor and neither the Issuer nor the Guarantor is aware of any such proceedings which are pending or threatened.

6. The financial statements of the Issuer and the Guarantor have been audited, without qualification thereon, in each case for the financial year ended on 31 March 2016 and the financial period ended on 31 March 2015 by Deloitte LLP, of One Trinity Gardens, Broad Chare, Newcastle upon Tyne NE1 2HF.

7. Copies of the following documents may be inspected at the registered office of the Issuer and the Guarantor during usual business hours on any weekday (Saturdays, Sundays and public holidays excepted) during the period of 12 months starting on the date on which this Prospectus is made available to the public as required by the Prospectus Rules made by the Financial Conduct Authority:

(i) the Memorandum and Articles of Association of the Issuer and the Guarantor;

(ii) the unconsolidated, audited financial statements of the Issuer for the financial period ended 31 March 2015 and the financial year ended 31 March 2016 and the auditors' report thereon;

(iii) the unconsolidated, audited financial statements of the Guarantor for the financial period ended 31 March 2015 and the financial year ended 31 March 2016 and the auditors' report thereon;

(iv) the Trust Deed; and

(v) the Paying Agency Agreement.

This Prospectus is available on the website of the Regulatory News Service operated by the London Stock Exchange at <http://www.londonstockexchange.com/exchange/news/market-news/market-news-home.html>

8. The Issuer does not intend to provide post-issuance information in connection with the Bonds.

9. The yield on the Bonds is 1.651 per cent. per annum. The yield is calculated as of the Issue Date of the basis of the issue price of the Bonds. It is not an indication of future yield.

10. The Bonds and Coupons will bear the following legend: "Any United States person who holds this obligation will be subject to limitations under the United States income tax laws, including the limitations provided in Sections 165(j) and 1287(a) of the U.S. Internal Revenue Code of 1986, as amended."

11. Certain of the Managers and their affiliates have engaged in, and may in the future engage in, investment banking and other commercial dealings in the ordinary course of business with the Issuer, the Guarantor and/or their respective affiliates. The Managers may have received, or may in the future receive, customary fees and commissions for these transactions.

In addition, in the ordinary course of their business activities, the Managers and their respective affiliates may make or hold a broad array of investments and actively trade debt and equity securities (or related derivative securities) and financial instruments (including bank loans) for their own account and for the accounts of their customers. Such investment and securities activities may involve securities and/or instruments of the Issuer, the Guarantor and/or their respective affiliates. Certain of the Managers or their respective affiliates that have a lending relationship with the Issuer and/or the Guarantor routinely hedge their credit exposure to the Issuer and/or the Guarantor, as applicable, consistent with their customary risk management policies. Typically, such Managers and their affiliates would hedge such exposure by entering into transactions which consist of either the purchase of credit default swaps or the creation of short positions in the relevant entity's securities, including potentially the Bonds. Any such short positions could adversely affect future trading prices of the Bonds. The Managers and their respective affiliates may also make investment recommendations and/or publish or express independent research views in respect of such securities or financial instruments and may hold, or recommend to clients that they acquire, long and/or short positions in such securities and bonds.



**REGISTERED OFFICE OF  
THE ISSUER AND THE GUARANTOR**

Northumbria House  
Abbey Road  
Pity Me  
Durham DH1 5FJ  
United Kingdom

**AUDITORS OF THE ISSUER AND THE GUARANTOR**

**Deloitte LLP**  
One Trinity Gardens  
Broad Chare  
Newcastle upon Tyne NE1 2HF  
United Kingdom

**LEGAL ADVISERS**

*To the Issuer and Guarantor*

**CMS Cameron McKenna LLP**  
Cannon Place  
78 Cannon Street  
London EC4N 6AF  
United Kingdom

*To the Managers and the Trustee*

**Linklaters LLP**  
One Silk Street  
London EC2Y 8HQ  
United Kingdom

**TRUSTEE**

**The Law Debenture Trust Corporation p.l.c.**  
Fifth Floor  
100 Wood Street  
London EC2V 7EX  
United Kingdom

**PRINCIPAL PAYING AGENT**

**HSBC Bank plc**  
8 Canada Square  
London E14 5HQ  
United Kingdom