ARTHUR ANDERSEN

Lennox Industries

Accounts 31 December 1998
together with directors' and auditors' reports

Registered number: 671868

Directors' report

For the year ended 31 December 1998

The directors present their annual report on the affairs of the company, together with the accounts and auditors' report, for the year ended 31 December 1998.

Principal activity and business review

The principal activity of the company continues to be the design, manufacture and sale of commercial heating and air conditioning equipment.

Turnover decreased by £2,634,988 (18%) during the year. The company made an operating loss of £2,529,415 (1997 - loss of £817,582) in the year.

No dividend is proposed for either the ordinary or preference shares for the year (1997 - £Nil).

Future developments

The company is committed to growth by focusing on core products, key customers and major markets in the UK and Ireland.

Directors and their interests

The directors who served during the year and subsequently were as follows:

J W Norris Jnr (USA) (Chairman)
P F Jolie (USA) (Managing Director) (Resigned 24 November 1998)
C W Wyant Jnr (USA)
R L Jenkins (USA) (Resigned 5 November 1998)
S Boxer (USA) (Appointed 5 November 1998)

The directors who held office at 31 December 1998 had no interests in the shares of the company which require disclosure under Schedule 7 of the Companies Act 1985.

Year 2000

The company has requested assurances from its software suppliers that its existing computer facilities are Year 2000 compliant. The company is confident that all other hardware and software is also Year 2000 compliant.

Directors' responsibilities

Company law requires the directors to prepare accounts for each financial year which give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing those accounts, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;

Directors' responsibilities (continued)

- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts; and

- prepare the accounts on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the accounts comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Auditors

The directors will place a resolution before the annual general meeting to reappoint Arthur Andersen as auditors for the ensuing year.

PO Box 174
Westgate Interchange
Northampton
NN5 5AG

By order of the Board,

W Burbidge

Secretary

31 March 1999

ARTHUR ANDERSEN

Auditors' report

Nottingham

To the Shareholders of Lennox Industries:

We have audited the accounts on pages 4 to 16 which have been prepared under the historical cost convention and the accounting policies set out on pages 6 to 8.

Respective responsibilities of directors and auditors
As described on pages 1 and 2, the company's directors are responsible for the preparation of the accounts. It is our responsibility to form an independent opinion, based on our audit, on those accounts and to report our opinion to you.

Basis of audit opinion
We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the accounts. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the accounts and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the accounts are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the accounts.

Opinion
In our opinion the accounts give a true and fair view of the state of affairs of the company at 31 December 1998 and of its loss for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Arthur Andersen

Arthur Andersen
Chartered Accountants and Registered Auditors

Fothergill House
16 King Street
Nottingham
NG1 2AS

31 March 1999

Profit and loss account

For the year ended 31 December 1998

	Notes	1998 £	1997 £
Turnover	2	11,763,823	14,398,821
Changes in stocks of finished goods and goods for resale		(1,075,237)	(519,116)
Other operating expenses (net)	3	(13,193,930)	(14,589,733)
Loss on sale of property and other fixed assets		(24,071)	(107,554)
Operating loss		(2,529,415)	(817,582)
Finance charges (net)	4	(11,962)	29,023
Loss on ordinary activities before taxation	5	(2,541,377)	(788,559)
Tax on loss on ordinary activities	7	-	-
Retained loss for the financial year	17	(2,541,377)	(788,559)
Retained loss, beginning of year		(5,107,714)	(4,319,155)
Retained loss, end of year		(7,649,091)	(5,107,714)

All operations of the company continued throughout both years and no operations were acquired or discontinued in either year.

There were no recognised gains or losses in either year other than the retained loss for the financial year.

The accompanying notes form an integral part of this profit and loss account.

Balance sheet

31 December 1998

	Notes	1998 £	1997 £
Fixed assets			
Tangible assets	8	1,136,485	1,267,925
Investments	9	32,765	32,865
		1,169,250	1,300,790
Current assets			
Stocks	10	1,614,988	2,502,800
Debtors	11	2,622,289	5,374,983
Cash at bank and in hand		1,038,041	1,839,774
		5,275,318	9,717,557
Creditors: Amounts falling due within one year	12	(5,291,281)	(7,311,613)
Net current (liabilities) assets		(15,963)	2,405,944
Total assets less current liabilities		1,153,287	3,706,734
Provisions for liabilities and charges	13	(68,844)	(80,914)
Net assets		1,084,443	3,625,820
Capital and reserves			
Called-up share capital	15	314,040	314,040
Capital contribution account	16	5,898,734	5,898,734
Share premium account	16	2,520,760	2,520,760
Profit and loss account	16	(7,649,091)	(5,107,714)
Total shareholders' funds	17	1,084,443	3,625,820
Shareholders' funds may be analysed as:			
Equity interests		784,443	3,325,820
Non-equity interests	15	300,000	300,000
		1,084,443	3,625,820

Signed on behalf of the Board

S Boxer Director

31 March 1999

The accompanying notes form an integral part of this balance sheet.

Notes to accounts
31 December 1998

1 Accounting policies
The principal accounting policies are summarised below. They have been applied consistently throughout the year and the preceding year.

a) Basis of accounting
The accounts have been prepared under the historical cost convention and in accordance with applicable accounting standards.

b) Basis of consolidation
These accounts present information about Lennox Industries as a single undertaking, and not about its group. Consolidated accounts have not been prepared, as permitted by the exemptions given under Section 229 (2) of the Companies Act 1985, because the directors consider that consolidation of the company's subsidiary undertakings (which did not trade during the year) would have no material impact on the accounts.

c) Tangible fixed assets
Tangible fixed assets are shown at cost less accumulated depreciation. Depreciation is provided at rates calculated to write off the cost, less estimated residual value, of each asset on a straight-line basis over its expected useful life as follows:

Improvements to long leasehold	-	shorter of length of lease and useful economic life
Plant and machinery	-	5 - 10 years
Motor vehicles	-	4 years

d) Stocks
Stocks are stated at the lower of cost and net realisable value. Cost incurred in bringing each product to its present location and condition is based on:

Raw materials	-	purchase cost on a first-in first-out basis, including transport
Work-in-progress and finished goods	-	cost of direct materials and labour, plus a reasonable proportion of manufacturing overheads based on normal levels of activity.

Net realisable value is based on normal selling price, less further costs expected to be incurred to completion and disposal. Provision is made for obsolete, slow-moving or defective items where appropriate.

e) Taxation
Corporation tax payable is provided on taxable profits at the current rate.

Advance corporation tax payable on dividends paid or provided for in the year is written off, except when recoverability against corporation tax payable is considered to be reasonably assured. Credit is taken for advance corporation tax written off in previous years when it is recovered against corporation tax liabilities.

Notes to accounts (continued)

1 Accounting policies (continued)

e) Taxation (continued)

Deferred taxation (which arises from differences in the timing of the recognition of items, principally depreciation, in the accounts and by the tax authorities) has been calculated on the liability method. Deferred tax is provided on timing differences which will probably reverse, at the rates of tax likely to be in force at the time of reversal. Deferred tax is not provided on timing differences which, in the opinion of the directors, will probably not reverse.

f) Pension costs

The company operates pension schemes providing benefits based on final pensionable pay.

The two schemes operating are the Lennox Industries Staff Retirement Benefits Scheme for staff employees and the Lennox Industries Retirement Benefits Scheme for hourly paid employees. The assets of the schemes are held separately from those of the company, being invested with insurance companies. The amount charged to the profit and loss account is the estimated regular cost of providing the benefits accrued in the year, adjusted to reflect variations from that cost. The regular cost is calculated so that it represents a substantially level percentage of current and future pensionable payroll. Variations from regular cost are charged or credited to the profit and loss account over the estimated average remaining working life of scheme members.

Any difference between amounts charged to the profit and loss account and contributions paid to independent pension schemes is shown as a separately identified liability or asset in the balance sheet.

g) Foreign currency

Transactions denominated in foreign currencies are recorded in the local currency at actual exchange rates as of the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the year end are reported at the rates of exchange prevailing at the year end. Any gain or loss arising from a change in exchange rates subsequent to the date of the transaction is included as an exchange gain or loss in the profit and loss account.

h) Turnover

Turnover comprises the amounts receivable for goods and services provided in the normal course of business, net of trade discounts, VAT and other sales-related taxes.

i) Leases

Assets held under finance leases are initially reported at the fair value of the asset with an equivalent liability categorised as appropriate under creditors due within or after one year. The asset is depreciated over the shorter of the lease term and its useful economic life. Finance charges are allocated to accounting periods over the period of the lease to produce a constant rate of return on the outstanding balance. Rentals are apportioned between finance charges and reduction of the liability, and allocated to cost of sales and other operating expenses as appropriate. Hire purchase transactions are dealt with similarly, except that assets are depreciated over their useful lives. Rentals under operating leases are charged on a straight-line basis over the lease term, even if the payments are not made on such a basis.

1 Accounting policies (continued)

j) Investments

Fixed asset investments are shown at cost less provisions for permanent diminution in value.

k) Cash flow statement

The company has taken advantage of the exemption in Financial Reporting Standard Number 1 (Revised) not to prepare a cashflow statement as it is a wholly owned subsidiary of a company whose accounts in which the company is included are publicly available.

2 Turnover

All turnover was derived from the company's principal activity.

The analysis of turnover by geographical destination is as follows:

	1998 £	1997 £
United Kingdom	8,247,936	7,783,287
Rest of Europe	1,762,229	3,316,335
Other	1,753,658	3,299,199
	11,763,823	14,398,821

3 Other operating expenses (net)

		1998 £	1997 £
Raw materials and consumables		8,024,967	9,215,519
Staff costs		3,152,014	3,128,419
Depreciation	- on owned assets	294,384	277,235
	- on assets held under finance leases	-	20,685
Other operating charges		1,722,565	1,947,875
		13,193,930	14,589,733

4 Finance charges (net)

Investment income

	1998 £	1997 £
Other interest receivable and similar income	54,405	29,884

4 Finance charges (net) (continued)

Interest payable and similar charges

	1998	1997
	£	£
Loans from group undertakings	66,367	-
Finance leases	-	861
	66,367	861

Finance charges (net)

	1998	1997
	£	£
Interest payable and similar charges	66,367	861
Less: investment income	(54,405)	(29,884)
	11,962	(29,023)

5 Loss on ordinary activities before taxation

Loss on ordinary activities before taxation is stated after charging (crediting):

	1998	1997
	£	£
Hire of plant and machinery under operating leases	171,931	156,894
Other operating lease rentals	317,500	492,500
Other exchange loss/(gain)	72,108	(45,254)
Auditors' remuneration	13,250	13,000

Amounts payable to Arthur Andersen by the company in respect of non-audit services to the company was £8,000 (1997 - £7,000).

6 Staff costs

The average monthly number of employees (including executive directors) was:

	1998	1997
	£	£
Production	78	98
Sales and distribution	41	37
Administration	13	17
	132	152

6 Staff costs (continued)

Their aggregate remuneration comprised:

	1998	1997
	£	£
Wages and salaries	2,764,235	2,777,650
Social security costs	208,948	209,455
Other pension costs (see note 18)	178,831	141,314
	3,152,014	3,128,419

Directors' remuneration was as follows:

	1998	1997
	£	£
Emoluments	100,818	95,512

Pensions

No directors were members of the company pension schemes at either year end.

7 Tax on loss on ordinary activities

No corporation tax is payable for the year ended 31 December 1998 (1997 - £Nil) as the company has accumulated tax losses brought forward from prior periods which are available to carry forward against future trading profits.

The deferred tax asset in respect of the tax losses has not been recognised on the grounds of prudence.

8 Tangible fixed assets

	Improvements to long leasehold £	Plant and machinery £	Motor vehicles £	Total £
Cost				
Beginning of year	390,258	2,103,540	52,659	2,546,457
Additions	62,160	126,208	24,041	212,409
Disposals	-	(109,268)	(22,723)	(131,991)
End of year	452,418	2,120,480	53,977	2,626,875
Depreciation				
Beginning of year	186,010	1,051,638	40,884	1,278,532
Charge for the year	44,108	241,172	9,104	294,384
Disposals	-	(60,531)	(21,995)	(82,526)
End of year	230,118	1,232,279	27,993	1,490,390
Net book value				
Beginning of year	204,248	1,051,902	11,775	1,267,925
End of year	222,300	888,201	25,984	1,136,485

Included within the above are items of plant and machinery held under finance leases with a cost of £Nil (1997 - £205,263). The accumulated depreciation in respect of these assets was £Nil (1997 - £135,976).

9 Fixed asset investments

	1998 £	1997 £
Investments at cost	32,765	32,865

The company owns 100% of the ordinary share capital of Environheat Limited, a dormant company registered in England and Wales. The aggregate capital and reserves of Environheat Limited at 31 December 1998 were £32,765 (1997 - £32,765).

During the year the company sold 100% of the ordinary share capital of HCF-Lennox Limited, a company registered in England and Wales for £100. The aggregate capital and reserves of HCF-Lennox Limited at date of sale was £100.

Consolidated accounts have not been prepared for the group on the basis that there is no material difference between the company and group accounts.

Notes to accounts (continued)

10 Stocks

	1998	1997
	£	£
Raw materials and consumables	862,231	674,806
Finished goods and goods for resale	752,757	1,827,994
	1,614,988	2,502,800

The directors do not consider that the carrying value of stocks at the end of the year is materially different from replacement cost.

11 Debtors

	1998	1997
	£	£
Amounts falling due within one year:		
Trade debtors	2,338,139	4,519,906
Amounts owed by group undertakings	157,620	180,795
VAT	-	15,324
Prepayments and accrued income	126,530	658,958
	2,622,289	5,374,983

12 Creditors: Amounts falling due within one year

	1998	1997
	£	£
Obligations under finance leases	-	19,839
Trade creditors	376,351	713,013
Amounts owed to group undertakings	4,044,445	5,495,876
Taxation and social security	173,855	67,489
Accruals and deferred income	696,630	1,015,396
	5,291,281	7,311,613

Included in amounts owed to group undertakings is a loan due to Lennox International. This loan is repayable on demand with interest charged at 6%.

Notes to accounts (continued)

13 Provisions for liabilities and charges

	Warranty provision £
Beginning of year	80,914
Charged to profit and loss account in year	(12,070)
End of year	68,844

14 Deferred taxation

	Unprovided	
	1998 £	1997 £
Accelerated capital allowances	75,000	71,006
Effect of tax losses carried forward	(75,000)	(71,006)
	-	-

The company has accumulated tax losses brought forward from prior periods which are available to carry forward against future trading profits. The deferred tax asset in respect of the tax losses has not been recognised on the grounds of prudence.

15 Called-up share capital

	1998 £	1997 £
Authorised		
15,000 ordinary shares of £1 each	15,000	15,000
470,000 redeemable non-cumulative preference shares of £1 each	470,000	470,000
	485,000	485,000
Allotted, called-up and fully-paid		
14,040 ordinary shares of £1 each	14,040	14,040
300,000 redeemable non-cumulative preference shares of £1 each	300,000	300,000
	314,040	314,040

Non-equity shareholders' funds relate to non-cumulative preference shares which are entitled to 6% of profits available for distribution. These shares may, at the company's option, be redeemed at par either wholly or in part at any time. They also carry the right to priority of capital on winding up, but no voting rights are attached.

Notes to accounts (continued)

16 Reserves

	Capital contribution account £	Share premium account £	Profit and loss account £	Total £
At 1 January 1998	5,898,734	2,520,760	(5,107,714)	3,311,780
Financial loss for the year	-	-	(2,541,377)	(2,541,377)
At 31 December 1998	5,898,734	2,520,760	(7,649,091)	770,403

The capital contribution account arose from the conversion of certain losses and accrued interest payable to the ultimate parent company and is not considered by the directors to be distributable.

17 Reconciliation of movements in shareholders' funds

	1998 £	1997 £
Loss for the financial year	(2,541,377)	(788,559)
Opening shareholders' funds	3,625,820	4,414,379
Closing shareholders' funds	1,084,443	3,625,820

18 Financial commitments

a) Capital commitments

The company had no capital commitments at either year end.

b) Pension commitments

The pension cost charge for the year was £178,831 (1997 - £141,314) for the staff scheme and £Nil (1997 - £Nil) for the hourly paid scheme.

The pension cost is assessed in accordance with the advice of a professionally qualified actuary. The latest actuarial valuation was as at 1 January 1996 and used the projected unit method. The main actuarial assumptions for the Lennox Industries Staff Retirement Benefits Scheme were that (a) salaries would increase by 7.0% p.a., (b) pensions paid would increase by 3% p.a., and (c) the return on scheme investments would be 8.5% p.a.

In respect of the Lennox Industries Staff Retirements Benefits Scheme, the most recent actuarial valuation showed that the market value of the scheme's assets was £2,796,949 and that the actuarial value of those assets represented 143% of the benefits that had accrued to members, after allowing for expected future increases in earnings. The latest actuarial review produced a cost in accordance with SSAP 24 of 6.1% of pensionable payroll consisting of a regular cost of 9.6% and a variation from regular cost of 3.5%.

Notes to accounts (continued)

18 Financial commitments (continued)

b) Pension commitments (continued)

In respect of the Lennox Industries Retirement Benefits Scheme for Hourly Paid Employees, the most recent actuarial valuation showed that the market value of the scheme's assets was £394,815 and that the actuarial value of those assets represent 225% of the benefits that had accrued to members, after allowing for expected future increases in earnings. This scheme was closed to new membership in January 1994. The remaining members still in the company's employment transferred to the staff scheme. No contributions are paid into the scheme.

c) Lease commitments

The company has entered into non-cancellable operating leases in respect of plant and machinery, the payments for which extend over a period up to 3 years. The total annual rental for 1998 was £171,931 (1997 - £156,894). The company also leases certain land and buildings on long-term operating leases. The annual rental on these leases was £317,500 (1997 - £492,500). The rents payable under these leases are subject to renegotiation at various intervals specified in the leases. The company pays for all insurance, maintenance and repairs to the properties.

The minimum annual rentals under the foregoing leases are as follows:

	Land and buildings		Other	
	1998	1997	1998	1997
	£	£	£	£
Expiring within one year	-	51,407	184,552	125,684
Expiring between two and five years	-	-	-	-
Expiring after five years	317,500	317,500	-	-
	317,500	368,907	184,552	125,684

19 Contingent liabilities

At 31 December 1998 the company had a bank guarantee of £220,000 (1997 - £220,000) in favour of Her Majesty's Customs & Excise, Deferment Section.

20 Transactions with related parties

The company has taken advantage of the exemption in Financial Reporting Standard Number 8 not to disclose related party transactions within the group as it is a wholly owned subsidiary of a company whose accounts in which the company is included, are available to the public. There were no other related party transactions.

21 Ultimate parent company and controlling party

Lennox Industries is a subsidiary of HCF Lennox Ltd, a company registered in England and Wales.

The results of Lennox Industries are consolidated within the results of LGL Netherlands BV. The accounts of LGL Netherlands BV are available to the public from LGL Netherlands BV, Watergoorweg 87, PO BOX 128, 3860 BA Nisker, The Netherlands.

21 Ultimate parent company and controlling party (continued)

The ultimate group of which Lennox Industries is a member and for which group accounts are drawn up is that headed by Lennox International Inc., the ultimate parent undertaking, a company registered in Iowa, USA. The accounts of Lennox International Inc. are not available to the public.

The ultimate controlling parties of the Lennox International Inc. group are the Norris and Booth families.