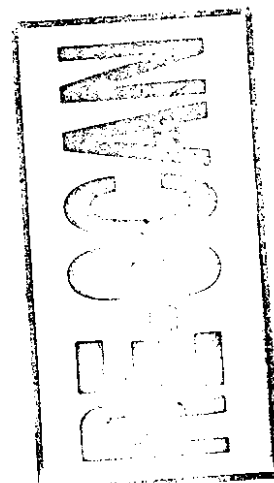


DIRECTORS' REPORT AND ACCOUNTS

LTS Rail Limited

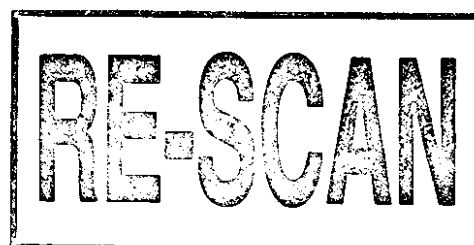
COMPANY No. 2938993

31 March 1998



Registered Office

Central House
Cliftown Road
Southend on Sea
Essex SS1 1AB



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Directors' Report and Accounts

LTS Rail Limited

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LTS Rail Limited

Directors' Report

The Directors submit their report and accounts for the year ended 31 March 1998.

Principal activity

The principal activity of the Company during the last financial year was the operation of passenger railway services between London Fenchurch Street and Shoeburyness. On 26 May 1996 the right to operate the Company's passenger railway services was franchised to Prism Rail PLC and on that date the Company became one of its wholly owned subsidiaries.

Business review and prospects

During 1997/8 passenger revenue rose by 10.4% to £60,637,000, and prospects for 1998/9 are promising. During the year the Company entered into an agreement with Porterbrook Leasing Limited for the lease of 44 four car electric multiple trains to be delivered by 1st November 1999. The first train is expected in late 1998. This will be the first time for many years that LTS will have received brand new trains. The placing of this order fulfilled a franchise commitment to the Office of Passenger Rail Franchising which resulted in the franchise being extended to 15 years.

Construction commenced during the year on a new station at West Ham which will connect with the Jubilee line extension, allowing LTS customers faster access to the West End of London. This is expected to open in the late summer of 1998.

Automatic ticket barriers were introduced at Barking station in September 1997 and an 18 month programme of installation at all the other stations served by the Company, together with closed circuit television, has now commenced.

Results and dividends

Details of the results are set out on page 6. The Company made distributable profits of £5,588,000 in the year. Interim dividends of £4,250,000 have been paid in the year with a further final dividend of £3,700,000 proposed.

Directors and their interests

The directors of the Company during the year were as follows:-

R Howells - Chairman
G Fearnley
K Bird
R McClean
H Nichol
M Powles (appointed 3 February 1998)
I Powney (resigned 21 July 1997)
N Wood (appointed 9 September 1997)

The interests of the Directors in the share capital and contractual arrangements with the Company and other group undertakings are disclosed in note 20.

LTS Rail Limited

Directors' Report (continued)

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 the Company and of the profit or loss of the Company for that period. In preparing these accounts the Directors are required to:-

- * select suitable accounting policies and then apply them consistently;
- * make judgements and estimates that are reasonable and prudent;
- * state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts;
- * 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 to 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.

Employees

LTS Rail Limited is a non-discriminatory employer operating an Equal Opportunities Policy which aims to eliminate unfair discrimination, harassment, victimisation and bullying. The Company is committed to ensuring that all individuals are treated fairly, with respect and are valued irrespective of disability, race, gender, health, social class, sexual preference, marital status, nationality, religion, employment status, age or membership or non-membership of a trade union.

The Company uses the consultative procedures agreed with its staff and elected representatives with a view to ensuring that employees are aware of the financial and economic factors which affect the Company's performance prospects.

The Company's policy is to continue to employ those who become disabled in service, together with some recruitment where circumstances permit. Training is adjusted to cater for an individual disability and the disabled share the same conditions of service as other staff in relation to career development and promotion.

Supplier payment policy

It is the policy of the Company to agree payment terms with suppliers or to make suppliers aware of standard payment terms at the time that orders for goods and services are placed, and settle accounts with suppliers in accordance with those terms, subject to satisfactory provision of the goods and services. Trade creditors at 31 March 1998 represented 35 days purchases (1997 : 32 days).

LTS Rail Limited

Directors' Report (continued)

Charitable and political contributions

The Company made charitable donations of £18,000 during the year.

Year 2000

Up to 31 March 1998, £115,000 had been incurred by the Company on millennium issues. It is estimated that a further £1,201,000 of expenditure will be incurred either directly or indirectly through the Company's participation in industry wide initiatives during the next two years, ensuring that all systems that it depends upon for its operation are millennium compliant.

Auditors

A resolution to re-appoint Solomon Hare as the auditors will be proposed at the Annual General Meeting.

On behalf of the Board.

A handwritten signature in black ink, appearing to read 'J P Simon'.

J P Simon
Secretary

Date: 17 June 1998

Auditors' Report to the Shareholders of

LTS Rail Limited

We have audited the accounts on pages 6 to 15 which have been prepared under the historical cost convention and on the basis of the accounting policies set out on pages 8 and 9.

Respective responsibilities of Directors and Auditors

As described on page 3, the Company's directors are responsible for the preparation of 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 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 as at 31 March 1998 and of the profit for the year then ended, and have been properly prepared in accordance with the Companies Act 1985.

Solomon Hare

Solomon Hare
Registered Auditors
Chartered Accountants
Oakfield House
Oakfield Grove
Clifton
Bristol BS8 2BN

17 June 1998

LTS Rail Limited

PROFIT AND LOSS ACCOUNT

Year ended 31 March 1998			Year ended 31 March 1997		
	Notes	£'000	Before exceptional items £'000	Exceptional items £'000	Total £'000
Turnover	2				
Passenger income		60,637	54,930	-	54,930
Revenue grant		27,728	24,245	-	24,245
Other income		<u>3,192</u>	<u>4,653</u>	<u>-</u>	<u>4,653</u>
		91,557	83,828	-	83,828
Operating expenditure	6	<u>(84,737)</u>	<u>(82,901)</u>	<u>(2,354)</u>	<u>(85,255)</u>
Operating profit/(loss)	3	6,820	<u>927</u>	<u>(2,354)</u>	(1,427)
Interest receivable & other investment income	7	1,686			1,014
Interest payable	7	<u>(4)</u>			<u>(2)</u>
Profit/(loss) on ordinary activities before taxation		8,502			(415)
Taxation	8	<u>(2,914)</u>			<u>-</u>
Profit/(loss) on ordinary activities after taxation		5,588			(415)
Dividends: paid		(4,250)			-
proposed		<u>(3,700)</u>			<u>-</u>
Retained loss for the year	18	<u><u>(2,362)</u></u>			<u><u>(415)</u></u>

All amounts relate to continuing activities.

There are no recognised gains or losses other than the profit for the year.

The notes on pages 8 to 15 form part of these accounts.

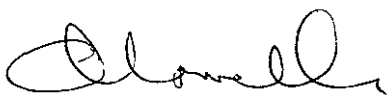
LTS Rail Limited

BALANCE SHEET
as at 31 March 1998

		31 March 1998 £'000	31 March 1997 £'000
Fixed assets	Notes		
Tangible fixed assets	9	1,581	453
Investments	10	<u>-</u>	<u>-</u>
		<u>1,581</u>	<u>453</u>
Current assets			
Stocks	11	537	576
Debtors	12	4,804	6,333
Cash at bank and in hand	13	<u>33,148</u>	<u>26,664</u>
		38,489	33,573
Creditors: Amounts falling due within one year	14	<u>(35,096)</u>	<u>(26,321)</u>
Net current assets		<u>3,393</u>	<u>7,252</u>
Total assets less current liabilities		4,974	7,705
Creditors: Amounts falling due after more than one year	15	(69)	(2)
Provisions for liabilities and charges	16	<u>-</u>	<u>(1,236)</u>
		<u>4,905</u>	<u>6,467</u>
Capital and reserves			
Called up share capital	17	1,000	800
Share premium account	18	3,000	2,400
Profit and loss account	18	<u>905</u>	<u>3,267</u>
Equity shareholders' funds	18	<u>4,905</u>	<u>6,467</u>

On behalf of the Board

Chairman:



R Howells

Managing Director:



K Bird

Date: 17 June 1998

The notes on pages 8 to 15 form part of these accounts.

LTS Rail Limited

**NOTES TO THE ACCOUNTS
for the year ended 31 March 1998**

1 Accounting Policies

The accounting policies of the Company are set out below:-

a) Basis of accounting

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

b) Turnover

- (i) Passenger income represents amounts agreed as attributed to the Company by the income allocation systems of the Rail Settlement Plan Limited, mainly in respect of passenger receipts. Income is attributed based principally on models of certain aspects of passengers' travel patterns and, to a lesser extent, from allocations agreed for specific revenue flows. The attributed share of season ticket income is deferred within creditors, and released to the profit and loss account over the period of the relevant season ticket.
- (ii) Revenue grant to 26th May 1996 relates to the Company's allocation from the British Railways Board of grants in respect of passenger services operated by the Company. After 26th May 1996 this item relates to amounts receivable from the Office of Passenger Rail Franchising. Income is recognised on an accruals basis.
- (iii) Other income is derived from ticket commissions, station trading income, depot and station access payments, performance regime payments, and the provision of goods or services to other train operating companies and excludes VAT. It is recognised on an accruals basis.

c) Tangible fixed assets and depreciation

Tangible fixed assets are stated at cost. Depreciation is provided on a straight line basis to write off the cost less estimated residual value of fixed assets over their expected useful economic lives as follows:-

Leasehold improvements	Shorter of the period of lease or franchise period
Plant and equipment	3 - 20 years (average 5 years)
Motor vehicles	4 years

d) Leased assets

Assets held under finance leases are included as tangible fixed assets and depreciated over their expected useful lives. The corresponding obligations relating to finance leases, net of finance charges allocated to future periods, are included in creditors. Finance costs are allocated to the profit and loss account on a straight line basis.

Operating lease rentals are charged to the profit and loss account on a straight line basis over the lease term.

LTS Rail Limited

NOTES TO THE ACCOUNTS (continued)

(e) Taxation

Deferred tax is calculated using the liability method in respect of timing differences arising from the difference between the accounting and tax treatment of various items. Provision is made where the timing differences are expected to reverse in the foreseeable future.

f) Stocks

Stocks are stated at the lower of cost and net realisable value.

g) Investments

Fixed asset investments are stated at cost less provision for any permanent diminution in value.

h) Pensions

The charge to the profit and loss account in respect of employees of the Company reflects the cost of pension obligations spread evenly over the working lives of the employees as recommended by the scheme's actuaries.

2 Turnover

All turnover was generated in the United Kingdom from the Company's principal activity, the operation of passenger rail services.

3 Operating profit/(loss)

The following amounts have been charged/(credited) in arriving at the operating profit/(loss):

	1998 £'000	1997 £'000
Auditors' remuneration		
Audit services	30	57
Non-Audit services	41	48
Track access charges payable to Railtrack PLC	35,955	38,591
Operating lease rentals:		
Rolling stock charges	17,223	16,122
Other plant and equipment	73	57
Other assets	129	255
Depreciation:		
Owned assets	108	108
Assets held under finance leases	-	-
Rents receivable	(884)	(793)
	<hr/>	<hr/>

LTS Rail Limited

NOTES TO THE ACCOUNTS (continued)

4 Directors' emoluments	1998	1997
	£'000	£'000
Aggregate emoluments	231	294
Compensation for loss of office	<u>68</u>	<u>60</u>
	<u><u>299</u></u>	<u><u>354</u></u>

The emoluments of the Chairman and one other director for services performed in connection with the Company were paid by Prism Rail PLC, the Company's parent undertaking, and recharged to the Company as part of a management charge.

Similarly, the emoluments of three other directors were paid by West Anglia Great Northern Railway Limited, a fellow subsidiary, and the proportion relating to services performed in connection with the Company recharged to the Company as part of a management charge.

The emoluments excluding pension contributions of the highest paid director were £97,000 (1997: £78,000). His accrued pension and accrued lump sum benefit as at 31 March 1998 was £40,567 and £37,838 respectively.

Retirement benefits accrued during the year to two directors under a defined benefit scheme in respect of services provided to the Company.

5 Employees	1998	1997
	£'000	£'000
Employee costs:		
Wages and salaries	12,400	13,126
Social security costs	944	1,001
Other pension costs	<u>348</u>	<u>359</u>
	<u><u>13,692</u></u>	<u><u>14,486</u></u>

The average number of persons employed by the Company during the year including directors was:	1998	1997
	Number	Number

Operations	598	608
Management and administration	<u>46</u>	<u>49</u>
	<u><u>644</u></u>	<u><u>657</u></u>

6 Exceptional items

The following exceptional items have been included in arriving at the operating profit:	1998	1997
	£'000	£'000
Restructuring and reorganisation costs	<u>-</u>	<u>2,354</u>

Restructuring and reorganisation costs represent expenses incurred in relation to the changes in organisational structure made and currently being implemented to facilitate the transition of the business to private ownership.

LTS Rail Limited

NOTES TO THE ACCOUNTS (continued)

7 Interest receivable and payable	1998	1997		
	£'000	£'000		
a) Interest receivable:				
Bank deposits	1,661	1,014		
Income from other investments	25	-		
	<u>1,686</u>	<u>1,014</u>		
b) Interest payable:				
Finance charges - finance leases	-	2		
Inter-group interest	3	-		
Other interest payable	1	-		
	<u>4</u>	<u>2</u>		
8 Taxation	1998	1997		
	£'000	£'000		
UK Corporation tax at 31%	2,478	-		
Tax charge on franked investment income	5	-		
Under provision for group relief payable in previous years	431	-		
	<u>2,914</u>	<u>-</u>		
9 Tangible fixed assets	Leasehold improvements	Plant and equipment	Motor vehicles	Total
	£'000	£'000	£'000	£'000
Cost				
At 1 April 1997	264	391	0	655
Additions	166	1,070	26	1,262
Disposals	-	-	(26)	(26)
At 31 March 1998	<u>430</u>	<u>1,461</u>	<u>-</u>	<u>1,891</u>
Depreciation				
At 1 April 1997	77	125	-	202
Charge for the year	<u>20</u>	<u>88</u>	<u>-</u>	<u>108</u>
At 31 March 1998	<u>97</u>	<u>213</u>	<u>-</u>	<u>310</u>
Net book value				
At 31 March 1998	<u>333</u>	<u>1,248</u>	<u>-</u>	<u>1,581</u>
At 31 March 1997	<u>187</u>	<u>266</u>	<u>-</u>	<u>453</u>

The net book value of assets held under finance leases and hire purchase agreements was nil (1996/7 - nil).

LTS Rail Limited

NOTES TO THE ACCOUNTS (continued)

10 Investments

The Company held the following unlisted investments at 31 March 1998 and 31 March 1997:

	Country of registration	Number of shares held	Class of share	Proportion held
ATOC Ltd	UK	1	Ordinary (4p)	4%
Rail Settlement Plan Ltd	UK	1	Ordinary (4p)	4%
Rail Staff Travel Ltd	UK	1	Ordinary (4p)	4%

These investments are shown at cost.

11 Stocks

	1998 £'000	1997 £'000
Engineering spares and consumable supplies	<u>537</u>	<u>576</u>

12 Debtors

	1998 £'000	1997 £'000
Trade debtors	2,175	3,729
Amounts owed by group undertakings:		
by parent undertaking	2	-
by fellow subsidiary undertaking	235	-
Other debtors	1,730	1,816
Prepayments and accrued income	<u>662</u>	<u>788</u>
	<u>4,804</u>	<u>6,333</u>

13 Cash at bank and in hand

Cash at bank and in hand includes an amount of £15,038,000 (1997: £15,140,000) held in a designated account to support a season ticket bond provided by the Company's bankers to the Director of Passenger Rail Franchising in support of the Company's franchise obligations.

14 Creditors: amounts falling due within one year

	1998 £'000	1997 £'000
Obligations under hire purchase and finance leases	-	1
Amounts owed to group undertakings:		
to parent undertaking	325	-
to fellow subsidiary undertaking	574	258
Trade creditors	6,722	7,788
Other creditors	2,412	1,200
Corporation tax payable	79	-
Group relief payable	2,687	-
Other taxation and social security	533	555
Proposed dividend	3,700	-
Deferred season ticket income	15,047	14,608
Accruals and other deferred income	<u>3,017</u>	<u>1,911</u>
	<u>35,096</u>	<u>26,321</u>

LTS Rail Limited

NOTES TO THE ACCOUNTS (continued)

15 Creditors: amounts falling due after more than one year	1998	1997
	£'000	£'000
Obligations under hire purchase and finance leases	-	2
Other creditors	69	-
	<u>69</u>	<u>2</u>

Obligations under hire purchase and lease finance are due as follows:

	1998	1997
	£'000	£'000
Within 1 year	-	1
Within 1 - 2 years	-	1
Within 2 - 5 years	-	1
	<u>-</u>	<u>3</u>

16 Provisions for liabilities and charges	1998	1997
	£'000	£'000
Restructuring provision	-	1236
	<u>-</u>	<u>1236</u>
Movements during the year were as follows:	1998	1997
	£'000	£'000
At 1 April 1997	1,236	-
Payments made	(338)	-
Transferred to group company	(105)	-
Transferred to creditors under one year	(663)	-
Transfer (to)/from profit and loss account	(130)	1,236
	<u>(130)</u>	<u>1,236</u>
At 31 March 1998	-	1,236

At 31 March 1998 deferred tax assets relating to accelerated capital allowances and other timing differences and not recognised in the accounts amounted to £425,000 (1997: £434,000).

17 Called up share capital	Authorised		Issued	
	Number	£	Number	£
	of shares		of shares	
Ordinary shares of 25p each				
At 1 April 1997	4,000,000	1,000,000	3,200,000	800,000
Issue of shares	-	-	800,000	200,000
	<u>-</u>	<u>-</u>	<u>800,000</u>	<u>200,000</u>
At 31 March 1998	<u>4,000,000</u>	<u>1,000,000</u>	<u>4,000,000</u>	<u>1,000,000</u>

Pursuant to an ordinary resolution passed at an Extraordinary General Meeting held on 1 October 1997, 800,000 ordinary shares were issued to Prism Rail PLC for a consideration of £1.00 per share.

LTS Rail Limited

NOTES TO THE ACCOUNTS (continued)

18 Reconciliation of movements in shareholders' funds

	Share capital	Share premium	Profit and loss account	Total
	£'000	£'000	£'000	£'000
At 31 March 1997	800	2,400	3,267	6,467
Share issue	200	600	-	800
Loss for the year	-	-	(2,362)	(2,362)
At 31 March 1998	<u>1,000</u>	<u>3,000</u>	<u>905</u>	<u>4,905</u>

19 Financial commitments

19 (a) Operating lease and similar commitments

The Company has the following annual commitments due under operating leases which expire as follows:

	1998		1997	
	Land & buildings	Other	Land & buildings	Other
	£'000	£'000	£'000	£'000
Under one year	-	-	-	284
Between one and five years	109	15,657	109	11,674
Over five years	-	92	-	7,298
	<u>109</u>	<u>15,749</u>	<u>109</u>	<u>19,256</u>

The Company has contracts with Railtrack PLC for access to the railway infrastructure (track, stations and depots), which are due to expire on 25 March 2003, 26 January 2004 and 31 March 2001 respectively. Lease and maintenance payments for the Company's 44 new air conditioned trains will commence with the first delivery in late 1998 and then increase with each subsequent delivery to £17,600,000 per annum. These agreements terminate with the franchise.

19 (b) Pension schemes

The majority of the Company's employees are members of the relevant shared cost section of the Railways Pension Scheme, a defined benefit scheme, which was established with effect from 1 October 1994 when the British Rail Pension Scheme was partitioned. The last actuarial valuation of the section for the Company was as follows:-

<u>Valuation date</u>	<u>Accrued liabilities & reserves (£'000)</u>	<u>Assets (£'000)</u>	<u>Funding level</u>
26 May 1996	19,000	21,800	114%

Contribution rates are determined based on independent actuarial valuations using the projected unit method. The principal assumptions underlying the latest valuation were that the long term average return on investments would exceed price inflation by 4% per annum, that future pensionable pay awards would exceed price inflation by 2% per annum, and that dividend growth on UK equities would be 0.5% per annum less than the rate of price inflation.

LTS Rail Limited

NOTES TO THE ACCOUNTS (continued)

20 Directors' interests

Mr R Howells and Mr G Fearnley have a beneficial interest in the shares of the ultimate parent company, Prism Rail PLC, and are also Directors of that company. Their interests in the shares of Prism Rail PLC are disclosed in the accounts of that company. No other director had an interest in the shares of the ultimate parent company.

Mr K Bird and Mr R McClean together with other senior management of the Company were allocated share options subject to certain qualifying conditions, as part of the Prism Rail PLC 1996 Unapproved Employee Share Option Scheme. The options over the shares held by these Directors was as follows:

	Date of grant	Number of shares	Exercise Price	Exercise date
K Bird	5 June 1996	50,000	205p	5 June 1999 to 4 June 2003
	11 September 1997	22,742	286.5p	11 September 2000 to 10 September 2004
R McClean	5 June 1996	10,000	205p	5 June 1999 to 4 June 2003
	13 June 1996	20,000	268p	13 June 1999 to 12 June 2003
	11 September 1997	13,586	286.5p	11 September 2000 to 10 September 2004

21 Related party transactions

The Company has taken advantage of the exemption from providing details of related party transactions with group related parties as they are incorporated within the accounts of its parent company, Prism Rail PLC. Copies of that company's accounts can be obtained from its registered office at 32 Ludgate Hill, London, EC4M 7DR.

22 Ultimate parent undertaking

The Company's controlling party and ultimate parent undertaking is Prism Rail PLC.

23 Cash flow statement

The Company has used the exemption under Financial Reporting Standard 1 not to prepare a cash flow statement as a consolidated cash flow statement is included in the accounts of its ultimate parent company.