LEBOEUF, LAMB, GREENE & MACRAE
L.L.P.
A LIMITED LIABILITY PARTNERSHIP INCLUDING PROFESSIONAL CORPORATIONS

'' YORK
HINGTON, D.C.
ANY
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RISBURG
TFORD
STON
KSONVILLE
ANGELES
ARK
SBURGH
T LAKE CITY
FRANCISCO

50 N. LAURA STREET
SUITE 2800
JACKSONVILLE, FL 32202-3650
(904) 354-8000
FACSIMILE: (904) 353-1673

WRITER'S DIRECT DIAL:

(904) 630-5342

LONDON
(A LONDON-BASED MULTINATIONAL PARTNERSHIP)
PARIS
BRUSSELS
MOSCOW
RIYADH
(AFFILIATED OFFICE)
TASHKENT
BISHKEK
ALMATY
BEIJING

December 6, 1999

FEDERAL EXPRESS
Ms. Blanca Bayo
Director, Division of Records
and Reporting
Florida Public Service Commission
2540 Shumard Oak Blvd.
Tallahassee, FL 32399-0850

991660 - WS

Re: Application of United Water Florida, Inc. for Transfer of Majority Organizational Control of its Corporate Grandparent, United Water Resources, Inc. to Lyonnaise American Holding, Inc.

Dear Sir:

Enclosed are the original and five copies of the Application of United Water Florida, Inc. for Transfer of Majority Organizational Control of its Corporate Grandparent, United Water Resources, Inc. to Lyonnaise American Holding, Inc. The required Notices are being mailed and published this week. Affidavits regarding notice will be late-filed exhibits. Also enclosed is the $6,000 filing fee for this application covering both water and wastewater utilities.

If you have any questions, please contact me at (904) 630-5342.

Sincerely,

Dan Richardson

Daniel D. Richardson

DDR:dtw
Enclosures

cc: without attachments:
John D. Williams
Billie B. Messer
Stephanie A. Clapp
Richard Redemann
D. Tyler Van Leuven, Esq.

137602

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Application of United Water Florida, Inc. for Transfer of Majority Organizational Control of its Corporate Grandparent, United Water Resources, Inc. to Lyonnaise American Holding, Inc.	)))))))	DOCKET NO. 991660-WS DATE SUBMITTED FOR FILING: December 7, 1999

APPLICANT

United Water Florida, Inc.
1400 Millcoe Road
Jacksonville, Florida 32239

Persons to contact concerning Application
Daniel D. Richardson or
Mallory Gayle Holm
LeBoeuf, Lamb, Greene & MacRae, L.L.P.
50 North Laura Street, Suite 2800
Jacksonville, FL 32202
(904) 354-8000

137601

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Application of United Water Florida, Inc. for Transfer of Majority Organizational Control of its Corporate Grandparent, United Water Resources, Inc. to Lyonnaise American Holding, Inc.	DOCKET NO. 991853-WS DATE SUBMITTED FOR FILING: DECEMBER 7, 1999

TO: **Director, Division of Records and Reporting**
Florida Public Service Commission
2540 Shumard Oak Blvd.
Tallahassee, Florida 32399-0850

The undersigned hereby makes application for the transfer of the majority organizational control of United Water Resources, Inc., the corporate grandparent of United Water Florida, Inc., the utility operating under Water Certificate No. 236-W and/or Wastewater Certificate No. 179-S located in Duval, Nassau, and St. Johns Counties, Florida, and submits the following information:

PART I **APPLICANT INFORMATION**

A) The full name (as it appears on the certificate*), address and telephone number of the seller: The "Seller" is the holder of the publicly held shares of United Water Resources, Inc., the corporate grandparent of the utility. The jurisdictional utility is:

United Water Florida, Inc.
Name of utility

(904) 721-4601 — Phone No.
(904) 721-4658 — Fax No.

1400 Millcoe Road
Office street address

Jacksonville — City
Florida — State
32239 — Zip Code

Post Office Box 8004 Jacksonville Florida 32239-8004
Mailing address if different from street address

* United Water Resources, Inc. holds no Florida certificates. Certificates are held in the name of United Water Florida, Inc.

B) The name, address and telephone number of the person to contact concerning this application:

Daniel D. Richardson | (904) 354-8000 | (904) 353-1673
Name | Phone No. | Fax No.

50 N. Laura Street, Suite 2800
Street address

Jacksonville | FL | 32202
City | State | Zip Code

C) The full name (as it appears on the certificate*), address and telephone number of the buyer:

Lyonnaise American Holding, Inc. ("LAH")
Name of utility

(201) 767-2851 | (201) 784-7067
Phone No. | Fax No.

2000 First State Boulevard
Office street address

Wilmington | DE | 19804-0507
City | State | Zip Code

same as street address
Mailing address if different from street address

n/a
Internet address if applicable

* Certificates from the Florida Public Service Commission are held in the name of United Water Florida, Inc.

D) The name(s) and address(es) of all of the buyer's corporate officers, directors, partners and any other person(s) who will own an interest in the utility.

100% of the outstanding capital stock of the buyer is held by Suez Lyonnaise des Eaux. A list of directors and officers of the buyer is attached hereto as Annex D-1, pages 9-10 of this Application.

PART II FINANCIAL AND TECHNICAL INFORMATION

A) Exhibit A - A statement by the buyer indicating how the transfer is in the public interest, including a summary of the buyer's experience in water and/or wastewater utility operations, a showing of the buyer's financial ability to provide service and a statement that the buyer will fulfill the commitments, obligations and representations of the seller with regard to utility matters. See pages 11-15 of this Application.

B) List the names and locations of other water and/or wastewater utilities owned by the buyer and PSC certificate numbers, if any. See Exhibit B, "About UWR, SLDE, and LAH", pages 16-18 of this Application.

C) Exhibit C - A copy of the purchase agreement. See bound draft Proxy Statement marked Exhibit C to this Application with Purchase Agreement included as Annex A therein.

D) Exhibit D - A statement of how the buyer is financing the purchase. See Exhibit D which is page 19 of this Application.

E) Exhibit E - A list of all entities, including affiliates, which have provided or will provide funding to the buyer, and an explanation of the manner and amount of such funding, which shall include their financial statements and copies of any financial agreements with the utility. This requirement shall not apply to any person or entity holding less than 10 percent ownership interest in the utility. See Exhibit D which is page 19 of this Application. Financial Statements are in the SLDE, LAH and United Water, Florida, Inc. 1998 Annual Reports which are marked as bound Exhibits E1, E2 and E3.

F) Exhibit F - A statement from the buyer that after reasonable investigation, the system being acquired appears to be in satisfactory condition and in compliance with all applicable standards set by the DEP. See Exhibit F which is page 20 of this Application.

If the system is in need of repair or improvement, has any outstanding Notice of Violation(s) of any standard(s) set by the DEP or any outstanding consent orders with the DEP, the buyer shall provide a list of the improvements and repairs needed and the approximate cost to make them, a list of the action taken by the utility with regard to the violations, a copy of the Notice of Violation(s), a copy of the consent order and a list of the improvements and repairs consented to and the approximate cost. See Exhibit F which is page 20 of this Application.

PART III <u>NOTICE OF ACTUAL APPLICATION</u>

A) Exhibit G - An affidavit that the notice of actual application was given in accordance with Section 367.045(1)(a), Florida Statutes, and Rule 25-30.030, Florida Administrative Code, by regular mail to the following:

(1) the governing body of the municipality, county, or counties in which the system or the territory proposed to be served is located;

(2) the privately owned water and wastewater utilities that hold a certificate granted by the Public Service Commission and that are located within the county in which the utility or the territory proposed to be served is located;

(3) if any portion of the proposed territory is within one mile of a county boundary, the utility shall notice the privately owned utilities located in the bordering counties and holding a certificate granted by the Commission;

(4) the regional planning council;

(5) the Office of Public Counsel;

(6) the Public Service Commission's Director of Records and Reporting;

(7) the appropriate regional office of the Department of Environmental Protection; and

(8) the appropriate water management district. Copies of the Notice and a list of entities noticed shall accompany the affidavit. THIS WILL BE A LATE-FILED EXHIBIT.

B) Exhibit H - An affidavit that the notice of actual application was given in accordance with Rule 25-30.030, Florida Administrative Code, by regular mail or personal delivery to each customer of the system being transferred. A copy of the Notice shall accompany the affidavit. THIS WILL BE A LATE-FILED EXHIBIT.

C) Exhibit I - Immediately upon completion of publication, an affidavit that the notice of actual application was published once in a newspaper of general circulation in the territory in accordance with Rule 25-30.030, Florida Administrative Code. A copy of the proof of publication shall accompany the affidavit. THIS WILL BE A LATE-FILED EXHIBIT.

PART IV FILING FEE

Indicate the filing fee enclosed with the application:

$3,000 (for water) $3,000 (for wastewater).

PART V OTHER

A) Exhibit J - Evidence that the utility owns the land where the utility treatment facilities are located. If the utility does not own the land, a copy of the agreement which provides for the long term, continuous use of the land such as a 99-year lease. The Commission may consider a written easement or other cost-effective alternative. See Exhibit J which is page 24 of this Application.

B) Exhibit K - The original and two copies of revised tariff sheet(s) reflecting the change in ownership. See Exhibit K which is page 25 of this Application.

C) Exhibit L - The utility's current certificate(s). If not available, an explanation of the steps taken to obtain the certificate(s). See Exhibit L which is page 26 of this Application.

PART VI **AFFIDAVIT**

I, Gary R. Moseley, do solemnly swear or affirm that the facts stated in the forgoing application and all exhibits attached thereto are true and correct and that said statements of fact thereto constitutes a complete statement of the matter to which it relates.

By: Gary R. Moseley
Applicant's Signature

Gary R. Moseley
Applicant's Name (Typed)

Vice President-General Manager
United Water Florida, Inc.
Applicant's Title

Subscribed and sworn to before me this 30th day of the month of ~~December~~ November in the year of 1999, by Gary R. Moseley, who is personally known to me ________________________ or produced the following identification ________________________________ (Type of Identification Produced).

Shannon J. Smith
Notary Public's Signature

NOTARY PUBLIC STATE OF FLORIDA
SHANNON JOY SMITH
MY COMMISSION # CC 807607
EXPIRES: 02/08/2003
1-800-3-NOTARY Fla. Notary Service & Bonding Co.

Print, Type or Stamp Commissioned Name of Notary Public

STATE OF NEW JERSEY)
) SS.:
COUNTY OF BERGEN)

JOSEPH V. BOYLE, being duly sworn, deposes and says that he is the Vice President – Finance and Treasurer of Lyonnaise American Holding, Inc., he has read the foregoing Application and knows the content thereof, and that the same is true to his own knowledge, information and belief.

Joseph V. Boyle

Sworn to before me this
29th day of November, 1999.

Debra Maureen Visconti
Notary Public

DEBRA MAUREEN VISCONTI
NOTARY PUBLIC OF NEW JERSEY
Commission Expires 8/19/2004

STATE OF NEW JERSEY)
) SS.:
COUNTY OF BERGEN)

DONALD L. CORRELL, being duly sworn, deposes and says that he is the Chairman, President and Chief Executive Officer of United Water Resources Inc., he has read the foregoing Application and the content thereof, and that the same is true to his own knowledge, information and belief.

Donald L. Correll

Donald L. Correll

Sworn to before me this
29th day of November, 1999.

Debra Maureen Visconti

Notary Public

DEBRA MAUREEN VISCONTI
NOTARY PUBLIC OF NEW JERSEY
Commission Expires 8/19/2008

ANNEX D-1

Directors and Executive Officers of LAH

Set forth below are the (i) name, (ii) current business address, (iii) present principal occupation or employment, (iv) material occupations, positions, offices or employments for the past five years and (v) citizenship of each director and executive officer of LAH.

Name and Current Business Address	Present Principal Occupation or Employment; Material Positions Held During the Past Five Years; Citizenship
Jerome Monod c/o Suez Lyonnaise des Eaux 1, rue d'Astorg 75008 Paris, France	Director and Chairman, LAH (1980-present); Chairman of the Supervisory Board, SLDE (1997-present); Chairman of the Board, Lyonnaise des Eaux (1980-1997). French citizen.
Philippe Brongniart c/o Suez Lyonnaise des Eaux 1, rue d'Astorg 75008 Paris, France	Director and President of LAH (1993-present); Member of the Executive Board, SLDE (1997-present); Executive Vice President, Lyonnaise des Eaux (1993-1997); Director, H\\2\\O Acquisition Co. (1999-present); President, LEO Holding Company (1999-present). French citizen.
Jean Michel Brault c/o United Water Services 200 Old Hook Road Harrington Park, New Jersey 07640-1799	Director and Executive Vice President, LAH (1997-present); Vice President-North America, SLDE (1994-present); Vice Chairman and Chief Executive Officer, United Water Services LLC (1997-present); Chairman and Chief Executive Officer, United Water Services Canada L.P. (1997-present); Chairman and Chief Executive Officer, United Water Services Mexico LLC (1997-present); Director and President, LAH Acquisition (1999-present); Vice President--Business Development, GTM International (SLDE subsidiary) (1992-1994). French citizen.

Thierry Bourbie c/o Suez Lyonnaise des Eaux 1, rue d'Astorg 75008 Paris, France	Director and Vice President, LAH (1998-present); Director, United Water Resources Inc. (1996-present); President of the International Water Division, SLDE (1996-present); Director of French Water Water Operations Lyonnaise des Eaux (1994-1996); Chief Executive Officer and Chairman, Lyd Informatique (SLDE subsidiary) (1994-1996); Chief Executive Officer and Chairman, Apic Syst (SLDE subsidiary) (1991-1995), Director, Sociedad General de Aguas de Barcelona, S.A. French citizen.
Joseph V. Boyle c/o United Water Services 200 Old Hook Road Harrington Park, New Jersey 07640-1799	Director, LAH (1997-present); Vice President-Finance and Treasurer, LAH (1994-present); Vice President, United Water Services LLC (1997-present); Vice President, LAH Acquisition (1999-present). United States citizen.

EXHIBIT A

Transfer of the majority organizational control of United Water Resources, Inc. ("UWR"), a New Jersey corporation and the grandparent corporation of United Water Florida, Inc., to Lyonnaise American Holding, Inc. ("LAH"), a Delaware corporation and the current owner and holder of 30.1% of the outstanding common stock and 98.1% of the preference stock of UWR (for purposes of this Application, the "Buyer"), is in the public interest.

Pursuant to an Agreement and Plan of Merger dated as of August 20, 1999 (the "Agreement"), by and among UWR, the Buyer, LAH Acquisition Co., a Delaware corporation and a wholly-owned subsidiary of the Buyer ("LAH Acquisition"), and Suez Lyonnaise des Eaux, a societe anonyme organized and existing under the laws of the Republic of France and the parent corporation of the Buyer ("SLDE"), UWR has agreed to merge with LAH Acquisition, with UWR as the surviving corporation. This merger will cause UWR to become a wholly-owned subsidiary of the Buyer; Buyer will thus increase its ownership of UWR to 100%. See the following Annexes attached hereto which explain and depict the subject transaction: Annex A-1, diagram of the pre-merger corporate organization of UWR, and Annex A-2, post-merger corporate organization of UWR. By virtue of the subject transaction, no change will occur in the ownership of UWR's indirect subsidiary, United Water Florida, Inc. ("UWF"), nor in its rates, conditions of service, or operations. See Proxy Statement with Agreement, Exhibit C.

As a result of the proposed transaction, UWR, the second largest water utility holding company in the United States, will become a wholly-owned subsidiary of the Buyer, which is itself a wholly-owned subsidiary of SLDE. See Exhibit B, "About UWR, SLDE and

LAH". Following the merger, the resulting company will continue to operate as United Water Resources, Inc. In keeping with its international business policy of allowing successful national firms to maintain their well-established national character, SLDE has announced that the management decision center for UWR will remain in Harrington Park, New Jersey which has been UWR's corporate headquarters for many years. No changes have been announced with respect to the operation of UWR's indirect subsidiary, UWF, or UWF's water or wastewater facilities as a result of the merger. Florida customers should continue to experience the same high quality of service that they have come to expect from UWF. All of the management expertise, experience, and strength of UWR will be retained. That management expertise, experience, and strength will be enhanced, however, by the world-wide strength of the Buyer and SLDE.

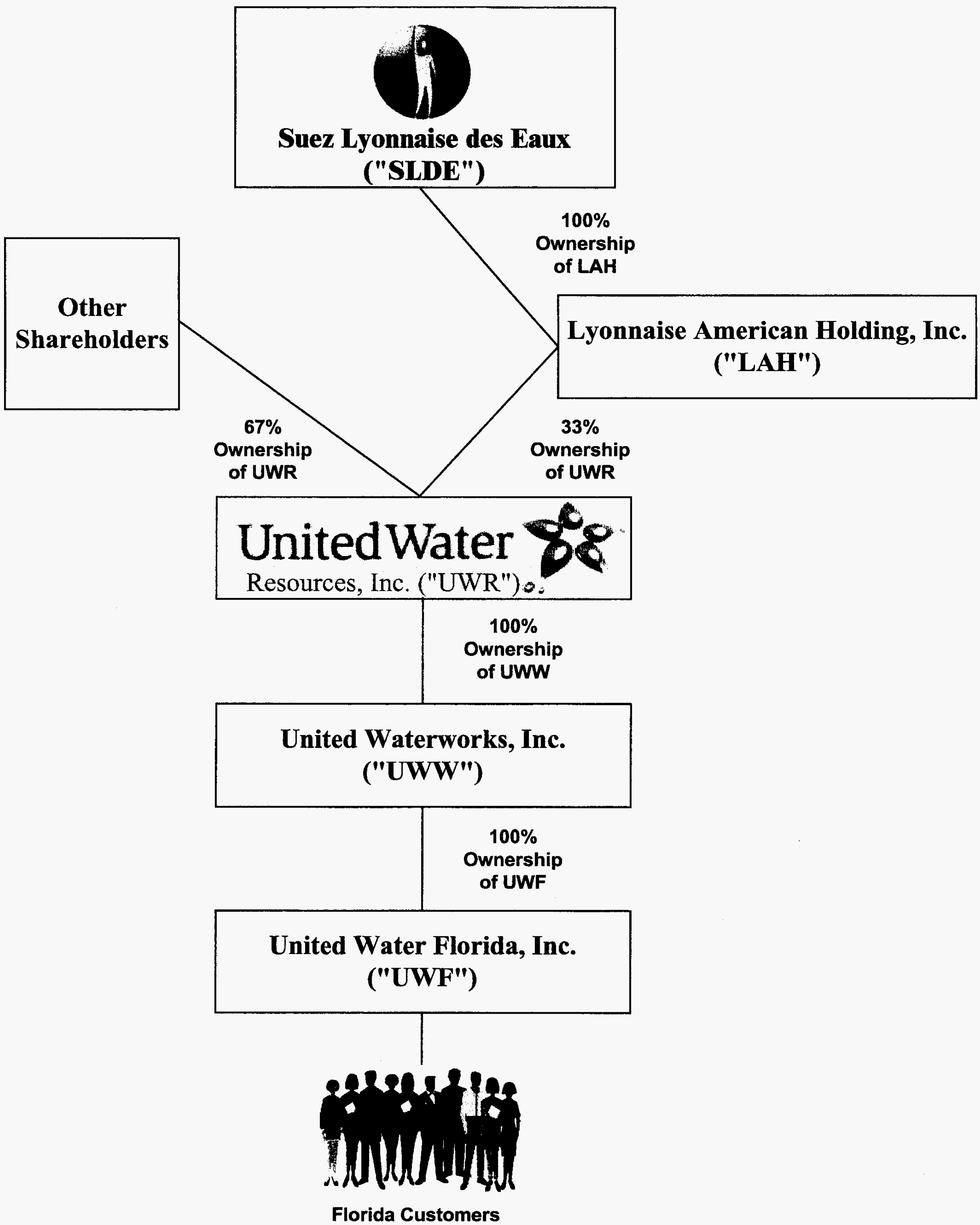
From a management and corporate point of view, the proposed transaction will significantly enhance UWF's position. As an indirect subsidiary of the Buyer, UWF, together with the other direct and indirect subsidiaries of SLDE, will have improved access to substantial financial, operational and technological resources. Those resources will allow UWF to continue to pursue the emerging opportunities for utility acquisitions and public/private partnerships in water and wastewater in Florida. UWF will be able to leverage the combined resources of UWR, the Buyer, and SLDE to meet the growing needs of its Florida municipal and industrial customers. UWF's access to greater financial resources will allow it to serve the public interest in Florida more effectively than ever before.

Another of the benefits of the proposed transaction that attracted UWR to the Buyer and its parent, SLDE, was the opportunity for more direct access to the advanced water quality expertise and world class research for which SLDE is famous. For instance, UWR and its subsidiaries have already benefitted from new technology developed by SLDE, including DNA chip technology for water testing, ultraviolet light disinfection, prefiltration and ultrafiltration, water recycling and iron removal. This transaction will further increase the capability of UWR and its subsidiaries to continue to provide high quality service and cutting edge technology to existing and new communities. SLDE's annual budget for research and development exceeds $60 million annually.

SLDE has vast experience in the successful planning and management of large capital projects. That experience will benefit the existing customers of UWR's wastewater and water utilities. It will also enhance UWR's capabilities which will be offered to future projects in Florida as the opportunities for growth present themselves.

The proposed transaction does not seek any changes in the rates charged by UWF to its customers, or in any of its policies with respect to service, employees, operations, financing, accounting, capitalization, depreciation or other matters affecting the public interest or utility operations. UWF will continue to maintain its books in accordance with the Uniform System of Accounts prescribed by the Commission. All commitments, obligations, and representations of UWR and UWF with regard to utility matters will continue to be fulfilled.

Ownership of United Water (Before Merger)



Ownership of United Water (After Merger)

Suez Lyonnaise des Eaux ("SLDE")

100% Ownership of LAH

Lyonnaise American Holding, Inc. ("LAH")

100% Ownership of UWR

United Water Resources, Inc. ("UWR")

100% Ownership of UWW

United Waterworks, Inc. ("UWW")

100% Ownership of UWF

United Water Florida, Inc. ("UWF")

Florida Customers

EXHIBIT B

ABOUT UWR, SLDE, AND LAH

United Water Resources Inc. (UWR)
200 Old Hook Road
Harrington Park, New Jersey 07640
(201) 784-9434

UWR is a holding company primarily engaged in water-related businesses. As the second largest investor-owned water services company in the United States, UWR provides water and wastewater services through its regulated utilities and nonregulated contract operations (some of which are owned jointly with the Buyer) to over 7.5 million people in more than 400 communities in 19 states. UWR also has investments in joint venture companies providing water services in Canada and Mexico, in which the Buyer is a majority owner, and has an investment in a water services company in the United Kingdom made in partnership with SLDE. In addition, UWR owns and manages real estate investments through a wholly-owned subsidiary. UWR has been listed on the New York Stock Exchange since 1889 and has paid cash dividends on its common stock continuously since 1886. See 1998 Annual Stockholder's Report.

Suez Lyonnaise des Eaux (SLDE)
1, rue d'Astorg
75008 Paris
France

SLDE, a societe anonyme organized and existing under the laws of the Republic of France, operates private infrastructure services in more than 120 countries, providing electricity and natural gas, waste services, communications services, and water services and maintains interests in construction and capital investments. SLDE was formed from the 1997 merger of Compagnie de Suez (builder of the Suez Canal) and Lyonnaise des Eaux. SLDE's registered office is located at 72 Avenue de la Liberte, 92022 Nanterre Cedex, France, and the principal address of SLDE's water division is 18 Square Edouard VII, 75316 Paris Cedex 09, France. See 1998 Annual Stockholder's Report.

Lyonnaise American Holding, Inc. (the Buyer)
2000 First State Boulevard
Wilmington, Delaware 19804-0507
(201)767-2851

The Buyer is a Delaware corporation. Its principal business is as a holding company of (i) its ownership interest in UWR, (ii) 50% of the voting interest in United Water Services LLC, a Delaware limited liability company which provides services in the water and wastewater industries to municipalities in the United States, (iii) majority interests in United Water Services Canada L.P., an Ontario, Canada limited partnership, and United Water Services Mexico LLC, a Delaware limited liability company, which provide services in the water and wastewater industries to municipalities in Canada and Mexico, respectively, and (iv) a 49% interest in Technologia y Servicios De Agua, S.A., a Mexican company which provides certain water services to the city of Mexico City, Mexico. On November 12, 1999, LAH acquired all of the Common Stock of Nalco Chemical Company ("Nalco"), through a newly created, wholly owned merger subsidiary for approximately 4.1 billion dollars. Nalco, based in Napezville, Illinois, is one of the world's largest providers of water treatment and process chemicals, services and systems.

All of the issued and outstanding shares of capital stock of the Buyer are owned beneficially and of record by SLDE. The principal business mailing address of the Buyer is c/o United Water Services LLC, 200 Old Hook Road, Harrington Park, New Jersey 07640, and the address of its principal office is 2000 First State Boulevard, Wilmington, Delaware 19804-0508. Annexed is the Consolidated Financial Statement for LAH for 1997 and 1998. (Exhibit E2.)

EXHIBIT D

STATEMENT OF HOW THE BUYER IS FINANCING THE PURCHASE

Under the terms of the Agreement, which has been approved by the Board of Directors of both companies, United Water Resources, Inc. will receive $35.00 in cash for each United Water Resources, Inc.'s share held. The transaction values all of the issued common shares of United Water Resources, Inc. at $1.36 billion ($0.90 billion for 67%). Suez Lyonnaise des Eaux will assume approximately $0.80 billion in net debt and preferred stock. The Agreement permits United Water Resources, Inc. to increase its regular quarterly dividend and to pay a special dividend at closing for an aggregate dividend increase of 48 cents per share. The total cash to be paid to United Water Resources, Inc.'s shareholders is $35.48, including the dividend increases, representing a premium of approximately 54% to United Water Resources, Inc.'s price of $23.06 on August 12, 1999. The transaction is expected to close during the first half of 2000.

Suez Lyonnaise des Eaux anticipates funding the United Water Resources, Inc.'s transaction from internal resources and existing bank facilities. Rothschild, Inc. and Rothschild & Cie have acted as financial advisors to Suez Lyonnaise des Eaux. Morgan Stanley Dean Witter and Co. acted as financial advisor to United Water Resources, Inc.

Energy

Water

Waste Services

Communications

SUEZ LYONNAISE DES EAUX *in 1998*

SUEZ LYONNAISE DES EAUX

CONTENTS

Suez Lyonnaise des Eaux sponsors an exhibition of Monet's Water Lilies at the Orangerie Museum in Paris

(organized by the Réunion des musées nationaux)

Claude Monet's trail-blazing "Nymphéas" or water lilies cycle marked a seminal moment in 20th century painting. He displayed the creativity and bold innovative spirit Suez Lyonnaise des Eaux seeks to promote in its own businesses, namely energy, water, waste services and communications. As in the world of the water lilies, where the beholder must look for the truth beneath the surface, where the fragile cycle of life first takes form, so, at the heart of life, Suez Lyonnaise des Eaux conceives, finances, builds and operates the world over.

Suez Lyonnaise des Eaux has produced an entertaining yet informative CD-Rom to take you on a "journey to the heart of life." Call freephone number (0800 177 177 in France) for your copy of this CD-Rom.

SUEZ LYONNAISE DES EAUX AT THE HEART OF LIFE

Energy, water, waste services, communications: Suez Lyonnaise des Eaux has chosen to focus its development on four services crucial to humanity's fundamental needs. Rapid urban growth, increasing demands for environmental protection and higher standards of service, market deregulation, growing recourse to private management, technological innovation–all these factors play a part in the massive upheavals occurring in our businesses at present, creating outstanding global opportunities for us.

Suez Lyonnaise des Eaux is transforming itself rapidly in order to respond to those challenges. It is turning itself into a worldwide group to provide the services customers demand. Today it is Europe's number one private electricity generator and world number three private energy producer; it is a world leader in the water management businesses; Europe's number one in waste management; the leading cable operator in France and Belgium. In all these sectors, Suez Lyonnaise des Eaux is confirming its position as a front rank player.

Having set out to generate 50 percent of its sales outside France and Belgium by 2002, the Group's ambition is to become the world leader in private infrastructure services, and to boost net current income per share to 8.54 euro (FRF 56 per share).

Revenues:
31.36 billion euro
(FRF 205.7 billion)
+ 8 percent

Capital expenditures:
15.5 billion euro
(FRF 101.7 billion)

201,000 employees
in 120 countries

Group net income:
1 billion euro (FRF 6.6 billion)
+ 64.3 percent

Group net current income:
0.76 billion euro (FRF 5 billion)
+ 25.2 percent

MESSAGE FROM THE CHAIRMAN AND FROM THE CEO AND PRESIDENT

JÉRÔME MONOD
CHAIRMAN OF THE SUPERVISORY BOARD

GÉRARD MESTRALLET
C.E.O. AND PRESIDENT OF THE EXECUTIVE BOARD

Dear shareholder,

Nineteen ninety-eight was the Suez Lyonnaise des Eaux Group's first full financial year.

When Compagnie de Suez and Lyonnaise des Eaux merged, in June 1997, we set ourselves a highly ambitious goal, which was to create a world leader in private infrastructure services.

At that time, we set ourselves three strategic aims:

- to re-center and streamline the Group around four core businesses, namely energy, water, waste services and communications;
- to make each of these businesses a global player;
- to reconcile growth with profitability in order to create value more pro-actively, our clear commitment being to double net current income per share by 2002.

We are pursuing this industrial project faithfully, rigorously, and with determination.

The results of the first two years confirm the Group's dynamism and potential, and have borne out the wisdom of the strategy you chose when you approved the merger.

Suez Lyonnaise des Eaux has accelerated its transformation into a truly industrial Group.

In the space of 24 months, the Group has definitively divested itself of its banking, financial and real estate activities in France. It now retains only a stable 21 percent stake in Fortis, Europe's tenth largest financial services group. Cross equity holdings with Saint-Gobain and Axa have been unwound, meanwhile.

OF THE SUPERVISORY BOARD OF THE EXECUTIVE BOARD

All of these transactions took place on excellent terms. The Group thus now enjoys substantial additional leeway, and the capital gains realized have boosted its earnings capacity. With 15.5 billion euro (FRF 101.7 billion) in investments and 6.5 billion euro (FRF 42.6 billion) in asset disposals in the past two years, Suez Lyonnaise des Eaux now ranks among France's foremost investors. Its cash flow 3.65 billion euro (FRF 24 billion in the 1998) has given it the means to reinforce its industrial capabilities.

Its core businesses now account for 68 percent of Group revenues and 73 percent of its capital employed.

Suez Lyonnaise des Eaux has established itself as a major worldwide player in its private infrastructure services businesses.

A number of significant acquisitions left their mark on 1998, notably BFI's international activities in waste services, and Gerasul, southern Brazil's number one electricity generator, in the energy sector.

The Group consolidated its positions in Europe and continues to conquer world markets.

In the energy sector, the Group has become the world's number three independent energy producer thanks to Tractebel. In Water, Suez Lyonnaise des Eaux is intensifying its business development, winning several new contracts. The successful integration of BFI's assets in 1998 and the acquisition in 1999 of the OTTO group, Germany's number three operator, have made us the leading waste services operator in Europe, Asia, and Latin America.

With a 65 percent increase in international operations, the Group's core businesses have again confirmed their growth potential. The proportion of core businesses' sales generated outside France and Belgium rose from 27 percent to 37 percent, in line with our 50 percent target set for 2002. As a front-rank player in each of its businesses, Suez Lyonnaise des Eaux intends to leverage its strengths and expertise in order to expand in these fast-growing markets, and to take advantage of the trend to outsourcing of municipal services to specialist operators.

Finally, Groupe GTM continued to build up its concession operating and services activities relative to its construction business, achieving first-class results in the process. It thus confirmed its robust profitability and strong international presence.

1998 earnings significantly exceeded our forecasts, confirming the performance and profitability targets set at the time of the merger.

This earnings performance points to strong future growth. At one billion euro (FRF 6.6 billion), net income, Group share, has been multiplied by three in two years. Net current income, the Group's key indicator, has grown by 25 percent in 1998 to 763 million euro (FRF 5 billion), having risen by 50 percent in the past two years.

> “ The results of the first two years confirm the Group's vitality and potential, and the wisdom of the strategy you voted for when approving the merger. ”

We are fully confident in the solidity of these prospects. Visibility over the next two years is strong, thanks to recurring earnings in our core businesses and capital gains from disposals already concluded.

Profitability and value creation are our priorities.

We confirm our target of doubling net current income per share to 8.54 euro (FRF 56) by 2002.

As pledged in 1997, we now have in place a series of indicators to analyze Group profitability. The overriding criterion is return on capital employed after tax, our medium-term objectives being to exceed the weighted average cost of capital plus three percentage points. This objective has indeed been incorporated into the formula used to calculate the remuneration of the Group's top management.

Our clearly-stated ambition is to turn our Group into one the market's top performers, a truly global Group in terms of its workforce, its markets, and its culture; to create a more coherent, more mobile and more dynamic Group, built upon a powerful, profitable presence in Europe.

We have reorganized our businesses in order to strengthen them.

In the Energy sector, the Group is preparing for market liberalization and radical changes impending in Europe, the United States and Latin America. The disposal of Elyo to SGB marked the first stage in the construction of a unified energy arm with Tractebel as its industrial focal point, in a drive to build a world-class energy business. That is our major industrial project for the coming months, as we start to create an operation covering the spectrum of electricity, gas, and heating technologies.

In the Water sector, our know-how lies in the management and operation of large-scale integrated drinking water distribution and waste water treatment systems. We intend to consolidate our world leadership in this industry.

In Waste Services, we have achieved our stated aims of growth and profitability.

In Communications, the Group is now the leading shareholder of TPS. It is accompanying the vigorous development of M6, and is positioning Lyonnaise Câble on the new digital and multimedia markets.

We have organized the Group along more forceful lines, working through more tightly-knit management teams.

Training, human resources management, and new, more modern, more international working methods... we have set in motion several programs to adapt the Group rapidly and effectively to globalization and the new demands made by its markets. For example, we have set up an international university, to provide training of a standard and dimension to match our ambitions.

“ Visibility over the next two years is strong, thanks to recurring earnings in our core businesses and capital gains from disposals already concluded. ”

We wanted to bring the interests of our employees and shareholders full into line by giving our staff a stronger stake in the development of the Group, through our employee shareownership plans.

Suez Lyonnaise des Eaux also completed its review of its values this year. Professionalism, partnership, teamwork, value creation, protecting the environment, and ethics: those are the 6 values that unite our 201,000 employees around the world, and to which they are committed.

At the dawn of the 21st century, Suez Lyonnaise des Eaux was born with high ambitions, namely to imagine, finance, build and operate what is at the heart of humans' most fundamental needs the world over.

Designing rational, efficient energy systems, supplying water to all, managing urban waste services while respecting the environment those are some of the major challenges facing businesses and local governments. The Group has the skills and the resources to meet those challenges. Each of its employees is well aware of this ambition and strives to earn the confidence, customers and shareholders have placed in him or her.

We hereby renew our pledge to work for these objectives.

Very sincerely yours.

Jérôme Monod

JÉRÔME MONOD

GÉRARD MESTRALLET

CORPORATE GOVERNANCE

Suez Lyonnaise des Eaux rigorously and vigilantly applies the principles of corporate governance. In addition to the necessary compliance with the rules laid down by the financial markets supervisory authorities, the Group is careful to respect each of its shareholders, seeking to provide full and clear disclosure of all relevant information.

SUPERVISORY BOARD

Jérôme MONOD
68, Chairman of the Supervisory Board, Chairman of the Board (1997-2001).
French.

Jean GANDOIS
68, Vice Chairman of the Supervisory Board, Former President of the CNPF (French employers' confederation). Vice Chairman of the Board (1997-2001).
French.

Gerhard CROMME(1)
55, Chairman of the Executive Board, THYSSEN KRUPP AG (1997-2001).
German.

Etienne DAVIGNON
66, Chairman, SOCIÉTÉ GÉNÉRALE DE BELGIQUE (1997-2001).
Belgian.

Paul DESMARAIS Jr(1)
44, Chairman of the Board and Co-Chief Executive, POWER CORPORATION OF CANADA (1998-2001).
Canadian.

Reto DOMENICONI(1)
62, Former Executive Vice President, NESTLÉ SA (1997-2001).
Swiss.

Lucien DOUROUX
65, Chief Executive Officer, CAISSE NATIONALE DE CRÉDIT AGRICOLE (1997-2001).
French.

Jean DROMER (†)
69, Chairman, Fondation de France (1997-1998).
French.

Pierre FAURRE
56, Chairman, SAGEM (1997-2001).
French

Ricardo FORNESÀ RIBO
67, Chairman, SOCIEDAD GENERAL DE AGUAS DE BARCELONA SA (1997-2001).
Spanish.

Albert FRERE(2) (3)
72, Chairman, GROUPE BRUXELLES LAMBERT (1997-1999).
Belgian.

Frederick HOLLIDAY
63, Chairman, NORTHUMBRIAN WATER GROUP (1997-2001).
British.

Philippe JAFFRE(1)
53, Chairman and Chief Executive Officer ELF AQUITAINE (1997-2001).
French.

André JARROSSON
68, Honorary Chairman, Groupe GTM (19971-2001).
French.

Jacques LAGARDE(1)
60, Adviser to the Chairman, THE GILLETTE COMPANY (1997-2001).
French.

Philippe MALET(2)
73, Honorary Chairman, COMPAGNIE DES SALINS DU MIDI ET DES SALINES DE L'EST (1997-1999).
French.

Bernard MIRAT(1) (2)
71, Former Deputy Chairman and CEO, SOCIÉTÉ DES BOURSES FRANÇAISES (1997-1999). French.

Jean PEYRELEVADE
59, Chairman, CRÉDIT LYONNAIS (1997-2001).
French.

Claude PIERRE-BROSSOLETTE(2)
70, Chairman, CAISSE DE REFINANCEMENT HYPOTHÉCAIRE (1997-2000).
French

Jean SYROTA
61, Chairman, COGEMA (1997-2001).
French.

Patrick Billioud is Secretary to both the Supervisory Board and the Executive Board.

From left to right: Front row: Lucien Douroux, Jean Gandois, Jérôme Monod, Albert Frère, Jean Syrota. Middle row: Claude Pierre-Brossolette, Jean Peyrelevade, Etienne Davignon, Frederick Holliday, Gerhard Cromme. Back row: Reto Domeniconi, Jacques Lagarde, Pierre Faurre, Bernard Mirat, Philippe Malet. Not shown: Paul Desmarais Jr., Ricardo Fornesa-Ribo, Philippe Jaffré, André Jarrosson.

(1) Independent member: unsalaried, being neither an officer of Suez Lyonnaise des Eaux nor of a Group company, nor linked to one or more significant shareholders or customary partners of the Group or of a Group company.

(2) Having due regard to the statutory age limit, the statutory limit of a term being 4 years.

(3) Mandate to be put forward for renewal 1999.

The 20-member Supervisory Board is designated by the Shareholders' General Meeting and met 6 times in 1998. The Supervisory Board of Suez Lyonnaise des Eaux is one of the most international in Europe, with 7 non-French members. Six out of the 20 members are "independent" [1].
The company by laws require each member of the Supervisory Board to hold at least 400 shares. A total of 523,662 euro (FRF 3,435,000) was paid in Directors' fees in 1998 to members of the Supervisory Board and of the three sub-committees.
The Supervisory Board has established three sub-committees: Audit, Ethics, Nomination and Compensation. You may consult the reports of Committees of the Supervisory Board on page 154.

Board sub-committees:

The Audit Committee, chaired by Claude Pierre-Brossolette, met 3 times in 1998. The Suez Lyonnaise des Eaux Audit Committee performs two main functions. The first is to submit the half-yearly and annual financial statements to detailed scrutiny in order to enlighten the Supervisory Board as to their content and their presentation to the public. The second is to be apprised of internal and external control procedures, in order to ensure that they appropriately cover all areas at risk.
The Ethics Committee, chaired by Jacques Lagarde, met 4 times in the course of the year. It enforces compliance with the individual and collective values that underpin the activities of the Group, and the rules of conduct which each individual employee is required to apply.
The Nomination and Compensation Committee, chaired by Jean Gandois, met twice in 1998. It submits recommendations to the Supervisory Board regarding the nomination and remuneration of members of the Supervisory Board and the Executive Board.

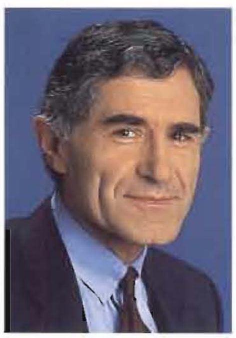
Executive Board

Appointed for 4 years, the 3-member Executive Board consists of:

Gérard MESTRALLET,
President of the Executive Board

Philippe BRONGNIART,
Member of the Executive Board

François JACLOT,
Member of the Executive Board


Gérard Mestrallet


Philippe Brongniart


François Jaclot

Bernard PRADES,
Executive Vice President, assisted by Valérie Alain, Director Corporate Relations

Patrick BUFFET,
Executive Vice President , responsible for Strategy and Development

Valérie BERNIS,
Special Advisor to the President of the Executive Board

Staff Managers

Valérie BERNIS:
Senior Vice President, Financial Communications

Thierry CHAMBOLLE:
Senior Vice President, Environment and Technology

Alain FABRY:
Senior Vice President, International Affairs

Dominique FORTIN:
Senior Vice President, Human Resources

Didier RETALI:
Senior Vice President, Finance

Gérard LAMARCHE:
Senior Vice President, Strategic Planning and Control

Jacques LAMBERT:
Senior Vice President, Corporate Sales

Vincent de LA VAISSIERE:
Senior Vice President, Corporate Communications

Philippe de MARGERIE:
Vice President, General Counsel

Henry MASSON:
Senior Vice President, Corporate Internal Audit

Jean-Pierre STANDAERT:
Senior Vice President
Legal and Tax

Management of direct subsidiaries

Michel BLEITRACH:
Chairman and Chief Executive Officer, Elyo

Jean-Louis BRAULT:
Chairman and Chief Executive, Officer, Groupe GTM

Alain HELLEQUIN:
Chairman and Chief Executive Officer, Lyonnaise Câble

Christian MAURIN:
Chairman and Chief Executive Officer, Degrémont

Xavier MORENO:
Chairman and Chief Executive Officer, Suez Industrie

Christine MORIN-POSTEL:
Chief Executive Officer, Chairman of the Management Committee, SGB

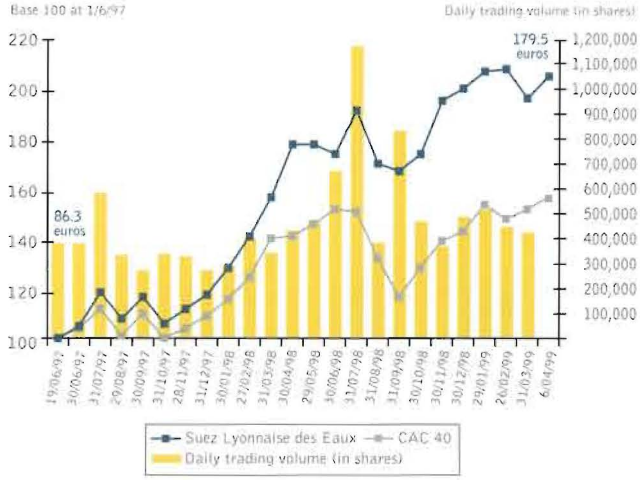
Gérard PAYEN:
Executive Vice President, Water Division

Jacques PETRY:
Executive Vice President Sita

SHAREHOLDERS' DIARY

There were 147.7 million Suez Lyonnaise des Eaux shares in issue at December 31, 1998, at a price of 175 euro (FRF 1,148). The public float represents 68 percent of the shares, and the average daily trading volume on the Paris Bourse was 430,000 shares. The Group's market capitalization exceeded 26.5 billion euro (FRF 174 billion) on April 6, 1999, when the price stood at 179.5 euro (FRF 1,177). The share price has gained 108 percent since the merger.

SHARE PRICE



Suez Lyonnaise des Eaux's share price has followed an upward trend since the merger, appreciating 108 percent, versus a 57 percent rise in the CAC 40 index of leading French stocks over the same period (19/06/1997 to 06/04/1999). **Suez Lyonnaise des Eaux was the fifth-best performing share in 1998.**

The share price rise was attributable to a series of major developments accomplished by the Group in 1998, as announced at the time of the merger in June 1997. These developments comprised recentering on the energy, water, waste services and communications businesses; accelerating the pace of international development; and improving earnings in each of the Group's businesses.

As a defensive growth stock, Suez Lyonnaise des Eaux has successfully weathered the recent bouts of stock market instability, confirming the favorable view taken of it by the markets.

SHARE DATA

• Suez Lyonnaise des Eaux shares are listed in:

Paris (monthly settlement market), Brussels, Geneva, Luxembourg. It is also traded on the Monep (Paris traded options market).

Sicovam ticker:	12052
Reuter ticker:	LYOE.PA
Bloomberg ticker:	LY FP

• Suez Lyonnaise des Eaux and EURO STOXX

Suez Lyonnaise des Eaux forms part of the Dow Jones EURO STOXX index, the broad euro index of 320 large cap stocks selected throughout the euro zone, ranking second in the "Utilities" subdivision.

• 1998 dividend

A dividend of 2.70 euro (FRF 17.71) per share, making a gross dividend of 4.05 euro (FRF 26.56) including tax credit, up 18 percent over the previous year's dividend, will be proposed to the General Meeting of Shareholders on May 28th, 1999.

Our commitments

- To double net current income per share in 5 years to 8.54 euros (FRF 56) per share in 2002,
- To distribute a net dividend (excluding tax credit) representing between 40 and 50 percent of Group net income.

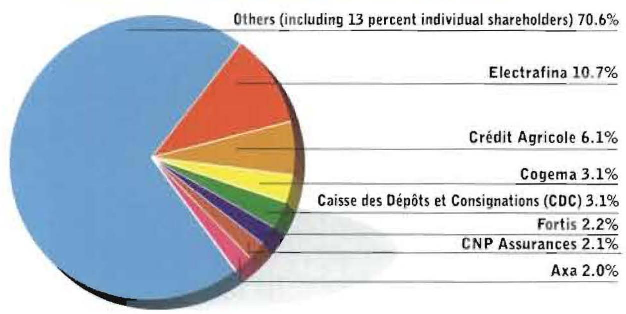
STOCK MARKET DATA

	1998		1997	
Price at 31/12	175 euro	FRF 1,148	101.5 euro	FRF 666
Number of shares in issue at 31/12	147,767,737		126,235,772	
Market capitalization at 31/12	26 billion euro	FRF 170 billion	13 billion euro	FRF 84 billion
Consolidated net income per share	7.4 euro	48.6 FRF	4.9 euro	FRF 32.3
Net dividend	2.70 euro	17.7 FRF	2.29 euro	FRF 15.0
Gross dividend	4.05 euro	26.6 FRF	3.43 euro	FRF 22.5
Total yield	2.31 percent		3.38 percent	

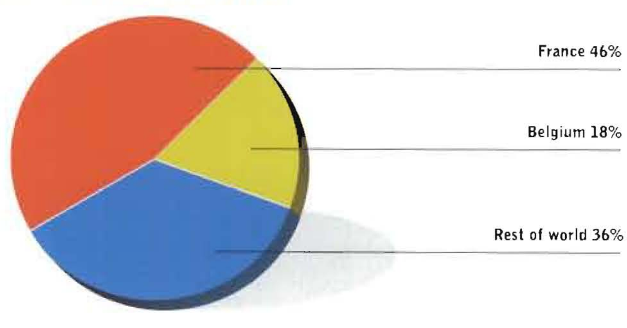
• Per share data

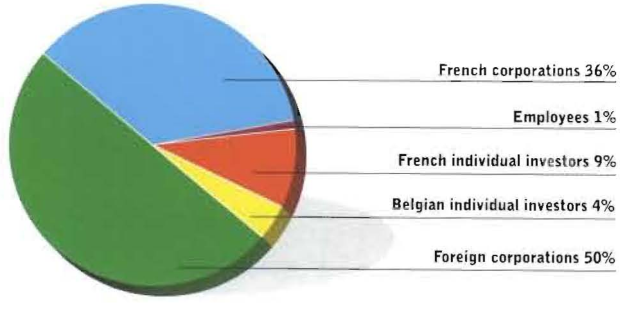
Par value:	10 euros
Number of shares in issue at December 31, 1998:	147,767,737
Group net current income:	5.6 euros (FRF 36.86)
Group net income per share:	7.4 euros (FRF 48.61)

SHAREOWNERSHIP AT 29/01/1999



SHAREOWNERSHIP





A WIDE DIVERSITY OF INDIVIDUAL SHAREHOLDERS

Because of its position and outlook, Suez Lyonnaise des Eaux's shares attract a wide diversity of investors.

Its 300,000 individual shareholders hold nearly 13 percent of its capital, representing an investment of more than 3.36 billion euro (FRF 22 billion).

- **Average holding:** : 52.41 shares, representing an average line of 9,507.20 euro (FRF 62,363), a rise of 58.1 percent over the average holding in 1997.
- **Geographic location:** 67 percent of shareholders live in the provinces.
- **Sex:** 44 percent of shareholders are male, 32 percent female, and 24 percent have joint accounts.
- **Representativeness of French shareownership:** the Group's French shareownership has two origins (stemming from privatization in the case of Compagnie de Suez, and Lyonnaise des Eaux's status as a blue-chip stock handed down from generation to generation). Consequently, the Group's individual shareholders cover a wide variety of profiles, comprising small investors (30 percent hold fewer than 11 shares) and holders of larger portfolios (11 percent hold more than 100 shares, representing a line exceeding 19,400 euro or FRF 127,000.

According to a survey by La Tribune/Sofres in July 1998 on a representative sample of 511 individual shareholders:

- 47 percent of them intend to hold onto their Suez Lyonnaise des Eaux shares;
- 45 percent want to buy Suez Lyonnaise des Eaux shares,
- 8 percent plan to sell.

They view Suez Lyonnaise des Eaux as an attractive investment:

- 30 percent consider the company's high profile is its main asset,
- 18 percent think its profitability and earnings make it a solid group,
- 15 percent appreciate its growth potential.

Creating value

Together with recentering, growth and development, value creation has been a priority right from the birth of Suez Lyonnaise des Eaux.
It is an integral part of the Group culture. Today, it is a state of mind shared throughout all Group subsidiaries.
It guides the Executive Board in its strategic decisions, and shapes the efforts of every member of Group personnel.

Each year, in June, each subsidiary draws up its own five-year plan. This is when they reaffirm their growth strategy and spell out how they intend to achieve their goals. The aim of each plan is to increase the subsidiary's contribution to Group earnings and optimize its use of resources.

The medium-term plans drawn up by the subsidiaries are then synthesized in the action plans for each operating division.

At the beginning of each year divisional managers define a target for return on capital employed (ROCE) in consultation with the Executive Board, and the Group has put in place a system of remuneration indexed on how successful these managers are in achieving their targets.

Similar systems are gradually being introduced in the various subsidiaries. At the same time, the number of beneficiaries of the stock options program was expanded in 1998.

Divisional managers thus have a stake in results alongside the Executive Board, and this is allowing shareholders in Suez Lyonnaise des Eaux to reap the full benefits of the Group's policy of recentering on its core businesses.

The outcome of this approach was a 12.3 percent return on equity in 1998, compared with 8.5 percent in 1997. Group net current income, mean while, advanced 25 percent, with a 15 percent rise on a per share basis. This pace of growth is consistent with the Group's goal of doubling this figure over the period 1997-2002.

With recentering practically completed, the Group is now concentrating on faster, profitable growth in its core businesses, as illustrated by the acquisition by Sita of BFI's non-North American operations, and those of Gerasul by Tractebel.

The challenge to Suez Lyonnaise des Eaux and to each of its subsidiaries is to combine rapid growth with value creation, and to do so in businesses characterized by long payback times on investments made today.

The key to the Group's capacity to create value for its shareholders lies in its pledge to:

- maintain its policy of improving margins and optimize returns on capital employed,
- select investments rigorously,
- preserve its financial flexibility thanks to a strong balance sheet, leaving the Group free to seize all investment opportunities if they are beneficial to shareholders.

Improving operating margins and optimizing returns on capital employed

The Group pursued its efforts to improve its operating margins in 1998. In the water sector, in France, a cost-cutting and purchasing optimization program was launched which is expected to achieve gross annual savings of around FRF 400 million by 2002.

In Europe, in the waste services sector, Sita is seeking to achieve a gross operating margin of FRF 200 million by 2000, by maximizing synergy between the former BFI units and its own subsidiaries.

Other action plans have been implemented concurrently in the water sector in Britain and Argentina, and in electricity in Belgium.

The Group's approach to investment selection

Rigorous selection of investment projects is the shareholder's best guarantee of an appreciating investment in Suez Lyonnaise des Eaux.

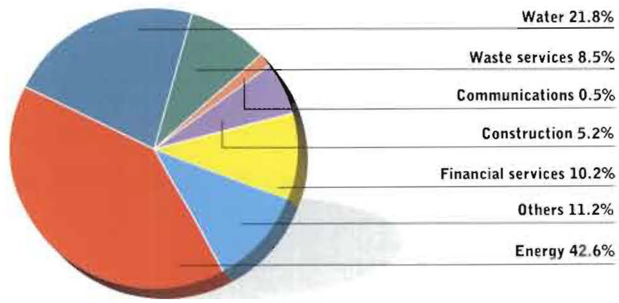
The investment selection committee, which is chaired by the Executive Board, approves a new project only after it has assured itself that the expected return is commensurate with the resources invested and a global assessment of the attendant risks.

The "shareholder's target rate of return" takes account

RETURN ON CAPITAL EMPLOYED 1998		NOPAT[1] (in euro billion)	CAPITAL EMPLOYED (in euro billion)
10%	**Core businesses**	**2.11**	**21.04**
10.8%	Energy	1.32	12.20
9%	Water	0.56	6.25
10.9%	Waste service	0.27	2.44
na	Communications	(0.04)	0.15
7.5%	**Other businesses**	**0.57**	**7.62**
9%	of which Construction	0.14	1.50
9.3%	**Group total**	**2.68**	**28.66**

[1] NOPAT : Net Operating Profit After Tax

Thanks to recentering, 73 percent of capital employed in 1998 was concentrated on the core businesses.



of the cost of the funds allocated by the Group to the project and the premiums required to remunerate the country risk, additional risks associated with the planned debt leverage, and any guarantees that the Group may be required to give.

The Executive Board further seeks to spread its geographic risks and the capital committed by the Group among its different businesses. It also hedges its investments against currency risk wherever necessary.

This responsibility is shared not only by each of the members of the Executive Board, but also by each project leader.

Once a project has been selected, it is included in the budget for the following year, and the compensation package of the manager concerned is adjusted accordingly.

Finally, the Group regularly monitors its international projects to ensure that expected contributions to earnings, and the planned optimization of Group resources upon which the decision was made, effectively materialize within the stipulated time frame.

Preserving adequate financial flexibility

With a debt-equity ratio of 59 percent, Suez Lyonnaise des Eaux has the leeway it needs to take advantage of new investment opportunities in its core businesses.

At the same time, however, the structure of this debt has altered substantially: thanks to its policy of recentering, the Group has significantly reduced the debt of its main companies, repaying high interest bank loans.

Conversely, the subsidiaries have optimized their balance sheets in order to close the gap between their debt and their cash flow.

The Group has increasingly sought to replace "corporate" debt by "project" debt.

The decision to call the 6.5 percent 1990 convertible bonds was one outcome of this reasoning. The scheduled launch of a new zero coupon FRF 5.2 billion bond issue convertible into AXA shares will further lower the Group's cost of capital.

At the same time as making its public exchange offer for SGB, the Group retired the securities released by the unwinding of its cross-shareholding with Saint-Gobain. This two-way transaction helped to boost the accretive impact of the operation for holders of Suez Lyonnaise des Eaux shares.

Finally, the Group's policy of repurchasing and retiring its shares has provided it with the wherewithal to optimize its profitability and boost its earnings per share.

To conclude, this strategy has placed the Group in a position to pursue its drive to maximize its return on capital employed in its core businesses.

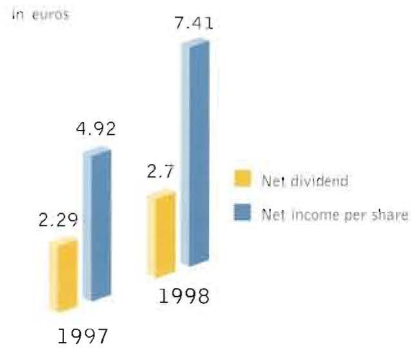
Today, these core businesses are generating rates of return of between 9 and 11 percent, yielding an average rate of return for the Group of 10 percent, which exceeds its weighted average cost of capital.

In pursuit of faster external growth, Suez Lyonnaise des Eaux is confident in its capacity to enhance shareholder value, and has set itself the target of exceeding its average cost of capital by 3 percent.

SUEZ LYONNAISE DES EAUX KEY FIGURES

A profitable strategy, now proving successful beyond its original commitments.
This strategy's three key goals in 1998 were: growth, recentering, and value creation.

Growth: revenues in our core business were up 17 percent in 1998. International revenues grew very strongly, rising 65 percent to 8 billion euro (FRF 52.6 billion).
Recentering: the Group's 4 core businesses now account for 68 percent of total revenues, 73 percent of capital employed, and 77 percent of EBITDA.
Value creation:
- return on capital employed (the benchmark for all investments) in the Group's core businesses was 10 percent after tax in 1998.
- Group net income has tripled in 3 years, from 0.3 billion euro (FRF 2 billion) in 1996 pro forma, to 1 billion euro (FRF 6.6 billion) in 1998.

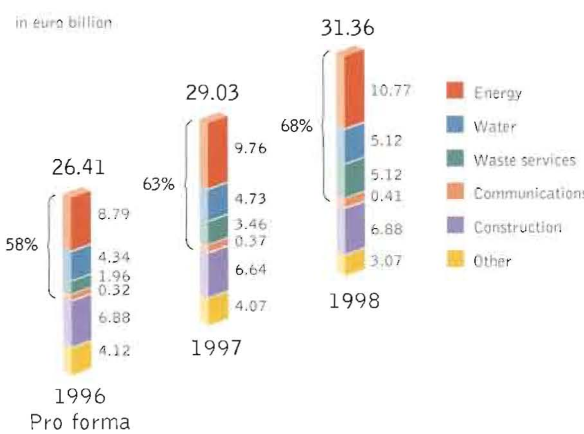


Another year of dividend growth: +18 percent over 1997.
Group earnings once more permit a further increase in the dividend for 1998 to 2.70 euro (FRF 17.7), versus 2.29 euro (FRF 15) in 1997. The net payout thus represents 52 percent of Group current net income.

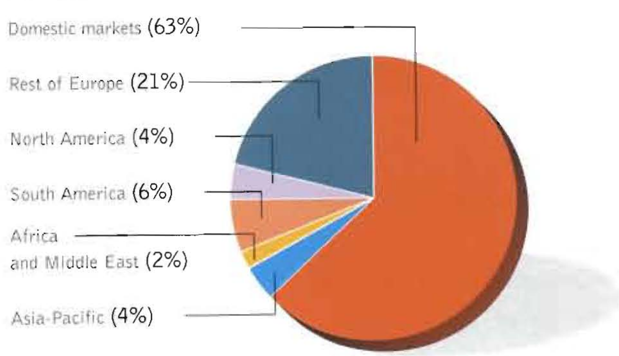
SIGNIFICANT REVENUE GROWTH

Revenues grew 8 percent relative to 1997, totaling 31.36 billion euro (FRF 205.7 billion) in 1998. At the same time, the core businesses increased their share of total revenues by 17 percent to 21.4 billion euro (FRF 140.5 billion, mainly thanks to the Group's continuing international expansion. Core business revenues outside France and Belgium rose 65 percent in 1998 and now account for 37 percent of total revenues generated by the core businesses (versus 27 percent in 1997). These results are in line with the Group's objective of boosting core businesses' international revenues to 50 percent of the total in 2002. All businesses are achieving significant organic growth, particularly the core businesses, which registered a 6.4 percent advance in 1998.

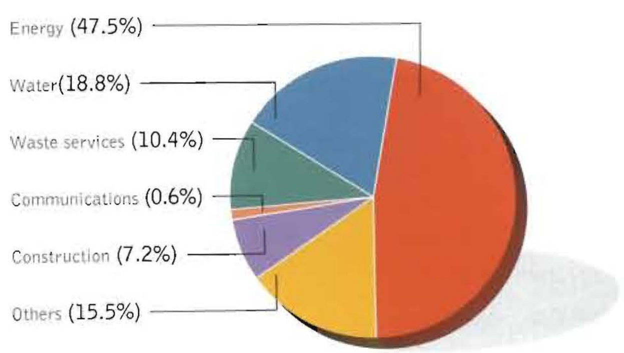
Core businesses increase their share of total revenues



Geographic breakdown of core business revenues, 1998.
Total: 21.42 billion euro (FRF 140.5 billion)



Total 1998 EBITDA: 6.12 billion euro



Improved profitability and a strong financial flexibility

EBITDA totaled 6.12 billion euro (FRF 40.2 billion) in 1998, of which 4.73 billion euro (FRF 31.1 billion), or 77 percent, was provided by our core businesses. EBITDA in our core businesses rose 9.3 percent relative to the previous year.

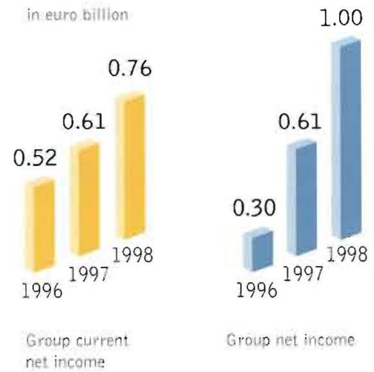
Group net income rose 64.3 percent over the year before to 1 billion euro (FRF 6.6 billion), having been multiplied by 3.3 in the past two years.

Net current income, meanwhile, advanced 25 percent to 763 million euro (FRF 5 billion). On a per share basis, the increase works out to 15 percent after accounting for the increase in the number of shares in issue (SGB public tender offer, which entailed the issuance of 25 million shares, and retirement of 4.8 million shares).

Group return on equity (ROE) has improved from 8.5 percent in 1997 to 12.2 percent in 1998.

The Group's debt-equity ratio was 59 percent at the end of 1998, with an interest/EBITDA cover of 7.5.

Group net income tripled in 3 years



Standard & Poor's rating

Suez Lyonnaise des Eaux's short-term paper is rated A-1 by Standard & Poor's, and its long term bonds are rated A+, by virtue of its "strong positions in several high cash-flow markets and its solid balance sheet". These rates are for its "strong positions in several high cash flow markets and its solid balance sheet".

Investment: 15.5 billion euro (FRF 101.7 billion) invested in 2 years (1997/1998)

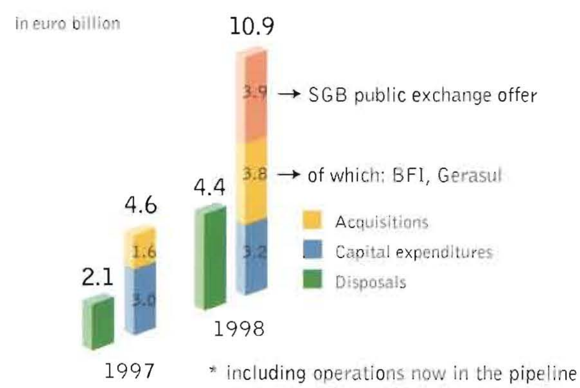
The Group has invested more than 15.5 billion euro (FRF 101.7 billion) in the space of 2 years (1997 and 1998).

Capital expenditures, together with acquisitions and equity investments, totaled 10.89 billion euro (FRF 71.4 billion) in 1998. Core businesses accounted for nearly 80 percent of this figure.

Of this figure, capital expenditures accounted for 3.15 billion euro (FRF 20.7 billion), and acquisitions and equity investments 3.76 billion euro (FRF 24.6 billion), plus 3.93 billion euro (FRF 25.8 billion) for the SGB public exchange offer.

At the same time, the Group has continued to sell off non-strategic assets. Disposals over the last two years (including operations begun in 1998, notably Sofinco and La Hénin Vie) total 4.38 billion euro (FRF 28.8 billion).

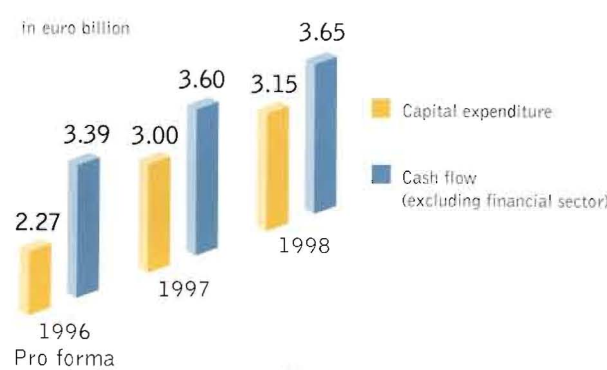
1997 and 1998 investment: 15 billion euro* (FRF 101.7 billion)



* including operations now in the pipeline

Cash flow, excluding the financial sector, totals 3.65 billion euro (FRF 24 billion). Core businesses generated 90 percent of this figure. This serves to finance capital expenditures (investment in plant modernization, and in measures to boost productivity and efficiency within the Group's industrial operations.

Substantial cash flow helping to finance the Group's vigorous growth



ALL SUEZ LYONNAISE DES EAUX FINANCIAL INFORMATION IS AVAILABLE ON: http://www.finance.suez-lyonnaise.com

SIGNIFICANT EVENTS

Suez Lyonnaise des Eaux continues to implement the strategy defined in 1997, the year of the merger between Suez and Lyonnaise des Eaux: streamlining, improving profitability, and internationalizing its core businesses.

Recentering, streamlining, and profitability

January

- Disposal of Suez Industrie's 27.7 percent shareholding in Prat Editions.
- Disposal of residual 24.4 percent shareholding in SEV.

April

- Public buyback tender offer for Elyo.
- Disposal of 100 percent shareholding in Banque Sofinco to Crédit Agricole Indosuez in two stages (70 percent in 1999 and 30 percent in 2000).
- Disposal of 3 office buildings, including former NMPP headquarters.

May

- Unwinding of cross shareholding with Saint-Gobain and announcement of retirement of 6.2 million Suez Lyonnaise des Eaux shares.
- Public exchange offer by Suez Lyonnaise des Eaux for Société Générale de Belgique, and public exchange offer by Fortis AG for Générale de Banque.

June

- Disposal of ISM by Crédisuez.
- Disposal of Société Hôtelière "Les Domaines du Soleil" by Crédisuez.

July

- Disposal by SGB of 55 percent shareholding in Recticel.
- Disposal of Banque La Hénin Epargne Crédit by Crédisuez.

September

- Disposal of la Foncière de l'Arcade by Crédisuez.

October

- Lyonnaise Câble disposes of its minority shareholdings in special interest channels.
- Retirement of 4.8 million Suez Lyonnaise des Eaux shares out of the 6.2 million announced.

December

- Early redemption of Suez Lyonnaise des Eaux 6.5 percent June 1990/ January 2000 convertible bonds.

January 1999

- Disposal of La Hénin Vie.
- Elyo Group restructures territorial organization in France.

April

- SGB acquires Suez Lyonnaise des Eaux's entire shareholding (100 percent) in Elyo.

Core businesses pursued their international development

ENERGY

January

- Trigen (54.4 percent subsidiary of Elyo) takes over Power Sources Inc (PSI), acquiring biomass expertise.
- Tractebel acquires electric power stations in Massachusetts, New Jersey, and California (640MW).

February

- Luxembourg: Electrabel wins contract to build and operate a 350MW combined gas-steam turbine electric power station at Esch-sur-Alzette.

April

- Portugal: Elyo inaugurates trigeneration power station at the site of the Lisbon World Fair.

May

- Tractebel and Electrebel acquire Scandic Energy, an energy trading company in Norway and Sweden.

August

- Tractebel signes concession project for the Cana Brava hydroelectric power station in Brazil (450MW, 35 years, start-up date: 2002).

In 1998, Tractebel acquired a 68 percent shareholding in Gerasul, the largest electricity producer in Southern Brazil.

Elyo built a trigeneration plant for the last Universal Exposition of the century, in Lisbon (Portugal).

September

- Brazil: Tractebel acquires a majority shareholding in electric power producer Gerasul (4,628MW).
- Poland: Elyo signs 12-year contract to design, upgrade, operate heating plants for the City of Poznan.

November

- Mexico: Tractebel wins 30-year renewable concession to distribute natural gas in the Queretaro region.
- Elyo acquires 75 percent controlling interest in Petrol Company, an energy management operator on the Italian market.

January 1999

- Tractebel raises its shareholding in Gerasul, Brazil (68 percent).

WATER

January

- United Water Services signs waste water treatment contract with Milwaukee, USA (28 municipal governments, 1.2 million inhabitants, 10 years).
- Degrémont world no. 1 in membrane ultrafiltration, signs contract with City of Del Rio (Texas, USA) to build an ultrafiltration plant; new drinking water plant for Lausanne (Switzerland).

March

- Lyonnaise des Eaux establishes global water technology research and development network: 2 new research centers established in the United Kingdom (NLTRC) and Asia Pacific (ASTRAN).
- China: Lyonnaise des Eaux wins contract to supply water to the City of Zhongshan: extension work and operation of 2 drinking water production plants for 22 years.
- San Antonio (Texas, USA): United Water Services signs 10-year contract to build and operate a drinking water plant using ultrafiltration technology.

April

- Degrémont acquires water treatment specialist Hager + Elsässer in Germany. This company notably specializes in ultrapure water for the microelectronics and pharmaceutical industries.
- Malaysia: Degrémont wins contract to build the Kota Tinggi station to supply drinking water to Singapore.

May

- Romania: 25-year BOT (Build, Operate, Transfer) contract with Bucharest, to build and operate a water treatment plant (1 million inhabitants).
- Indonesia: Lyonnaise des Eaux acquires 100 percent of GDS, which manages the water supply for western Jakarta.

June

- United Water Services wins 10-year waste water management contract for the City of Gary, Indiana (USA).
- Aéroport de Paris (Paris Airport Authority) awards contracts to build and operate the Roissy-Charles-de-Gaulle airport rainwater treatment plant to a consortium consisting of Lyonnaise des Eaux, Degrémont, Groupe GTM and Safège.
- United States: Degrémont wins two sludge incineration contracts for Northwest Bergen County (New Jersey) and Cincinnati (Ohio).

July

- Degrémont wins 9-year renewal of contract to operate the sludge treatment plant for Marseilles (France).
- Slovenia: Lyonnaise des Eaux and Degrémont sign contract to build and operate a waste water treatment station at Maribor (150,000 inhabitants) for 25 years.

Scale model of Cairo's future waste water treatment plant (Gabal el Asfar).

September

- Uzbekistan: Degrémont and Safège sign contract to supply water treatment equipment to the Samarkand Water Company (400,000 inhabitants).
- Hungary: Suez Lyonnaise des Eaux completes financing of acquisition of 25 percent shareholding the Budapest Water Company.
- China: Suez Lyonnaise des Eaux opens representative office in Beijing.
- China: signature of contract for construction by Degrémont of a waste water treatment plant for Shanghai.

October

- A USD 155 million investment company (LYLAW: Lyonnaise Latin America Water Corporation) formed with a pool of financial partners, to provide joint equity finance for the Group's Latin American projects in the production, treatment and distribution of water.
- Suez Lyonnaise des Eaux and Agbar increased their shareholding in Aguas Argentinas, Aguas de Santa Fé, and Aguas Cordobesas.
- Mexico: Degrémont activated the Ciudad Juarez BOT (build, operate, transfer) contract for the construction and operation of two municipal waste water treatment plants.

November

- Atlanta (USA): United Water Services (a 50/50 subsidiary of Suez Lyonnaise des Eaux and United Water Resources) won the biggest-ever delegated management drinking water contract signed in the United States (20 years, 1.5 million inhabitants).

December

- Egypt: Degrémont won the contract to build phase 3 of the Gabal el Asfar waste water treatment plant for the Cairo conurbation.

January 1999

- Italy: Suez Lyonnaise des Eaux won a 25-year contract to manage water supplies and waste water treatment for Arezzo (a syndicate of 27 municipal governments in Tuscany; 350,000 inhabitants).
- Jordan: Lyonnaise des Eaux won a 4-year contract water management and treatment contract for Amman (1.6 million inhabitants, with World Bank financing).

April 1999

- China: Suez Lyonnaise des Eaux won two new water contracts for Wanzhou and Changtu (plants to be built by Degrémont; Suez Lyonnaise des Eaux to operate them for 30 years).

WASTE SERVICES

February

- Signature of definitive contract to acquire all Browning-Ferris Industries (BFI) operations outside North America by Sita, representing a total investment of FRF 1.26 billion euro (FR F8.25 billion).

The shareholders of Sita are Suez Lyonnaise des Eaux (51.5 percent), BFI (19.2 percent), and the general public (29.3 percent). Sita is thus now the leading waste services company in Europe, Latin America, and Asia. The operation has allowed Sita to achieve critical mass in Germany and the Netherlands.

May

- Disposal to Faune of Sita's 49 percent shareholding in Grange SA, France's no. 1 manufacturer of domestic refuse trucks.

August

- Great Britain: Tractebel acquired A&J Bull, one of the largest waste services contractors in London.

December

- The waste services activities of Northumbrian Environment Management (NEM), a subsidiary of Northumbrian Water Group (NWG), were merged with those of Sita Holding UK.

The merger of the activities of NEM with those of Sita Holding confirmed Sita's no. 1 ranking on the UK waste services market (shown here, waste services workers in Bristol).

March 1999

- Sita holds 100 percent of the German OED Group.

Communications

February

- Lyonnaise Câble acquires 11 Absat channels for broadcasting on its own network.

May

- The Médiamétrie Audicabsat ratings ranked Cinestar, Cinétoile and Teletoon, broadcast by TPS, top of their respective theme-based channel categories (in cumulative audiences).

July

- Suez Lyonnaise des Eaux strengthened its communications sector organization. Alain Hellequin was named Chairman and CEO of Lyonnaise Câble and Senior Vice President of Suez Lyonnaise des Eaux, Multimedia and Cable Networks. A communications sector steering and development committee, chaired by Gérard Mestrallet, was formed.
- TPS and Absat sign a distribution and marketing agreement.

August

- The French Telecoms regulator issues a second ruling on the marketing of Internet access via cable in Paris. The 1.3 million Paris homes ready for connection in Paris can now enjoy the comfort and quality of broadband Internet access via Cybercable.

September

- TPS subscribers round the 500,000 mark.

October

- Lyonnaise Câble sells off its minority holdings in special interest channels (Planète, Ciné-Cinéma and Canal Jimmy) and raises its shareholding in Paris-Première. After having been present at the start-up of special interest broadcasting in France in the early 1990s, Lyonnaise Câble is now concentrating on development multiservice offerings on its cable networks.

- TPS and Thomson Broadcast Systems introduce "statistical multiplexing" for the first time in the Europe. This new broadcasting technology offers a 30 percent improvement in the digital quality of the image.

Nearly 700,000 homes have signed up to TPS satellite broadcasting system since its end-1996 launch

November

- TPS and Lagardère are selected by the Centre National d'Etudes Spatiales (French national space research center) and the Ministry of Education, Research and Technology, to broadcast multimedia educational services by satellite to 250 pilot sites.
- TPS launches "Espace Annonces," the first interactive small ad channel.
- Lyonnaise Câble launches its new interactive program guide for the 100,000 subscribers on its 25 cable networks.
- Suez Lyonnaise acquires the City of Paris' 23 percent shareholding in Paris TV Câble.

December

- TPS celebrates its second anniversary.

April 1999

- TPS subscribers round the 700,000 mark.

M6 was the only major national TV channel to gain ground in the under-50 age group in 1998, with a 17.8 percent audience share.

PRESENT IN 120 COUNTRIE

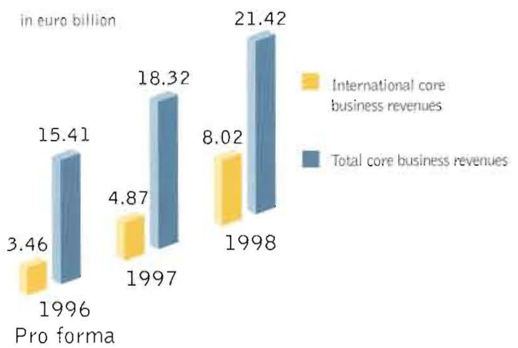
Suez Lyonnaise des Eaux does business in 120 countries, with a powerful presence in Europe.

The Group pursued its international expansion in 1998, and core business revenues rose 65 percent, accounting for 37 percent of total revenues, versus 27 percent in 1997.

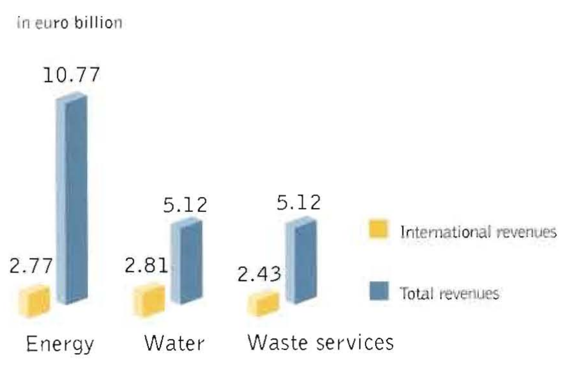
Suez Lyonnaise des Eaux selected data:

- 125 district heating systems in Europe (Elyo)
- 55 cities of more than 200,000 inhabitants served by Lyonnaise des Eaux
- 71 world capitals equipped by Degrémont
- 200,000 professional clients served by Sita
- 200 infrastructures in 67 cities built by Les Parcs GTM

International revenue growth



Share of international operations in the three main core businesses in 1998



ACCELERATED development in 1998

EUROPE

Netherlands, Sweden, Finland
Municipal waste collection and management (Sita), construction of an underwater rail tunnel linking Denmark and Sweden (Dumez-GTM).

Germany
Water management in Potsdam and Rostock (Lyonnaise des Eaux), water treatment (Degrémont).

Great Britain
Northumbrian Group water companies (Lyonnaise des Eaux), water treatment (Degrémont), waste services (Sita and Fabricom), operation of the Severn link (Groupe GTM), construction of high-speed rail infrastructures (Dumez-GTM), road building and maintenance (Entreprise Jean Lefebvre).

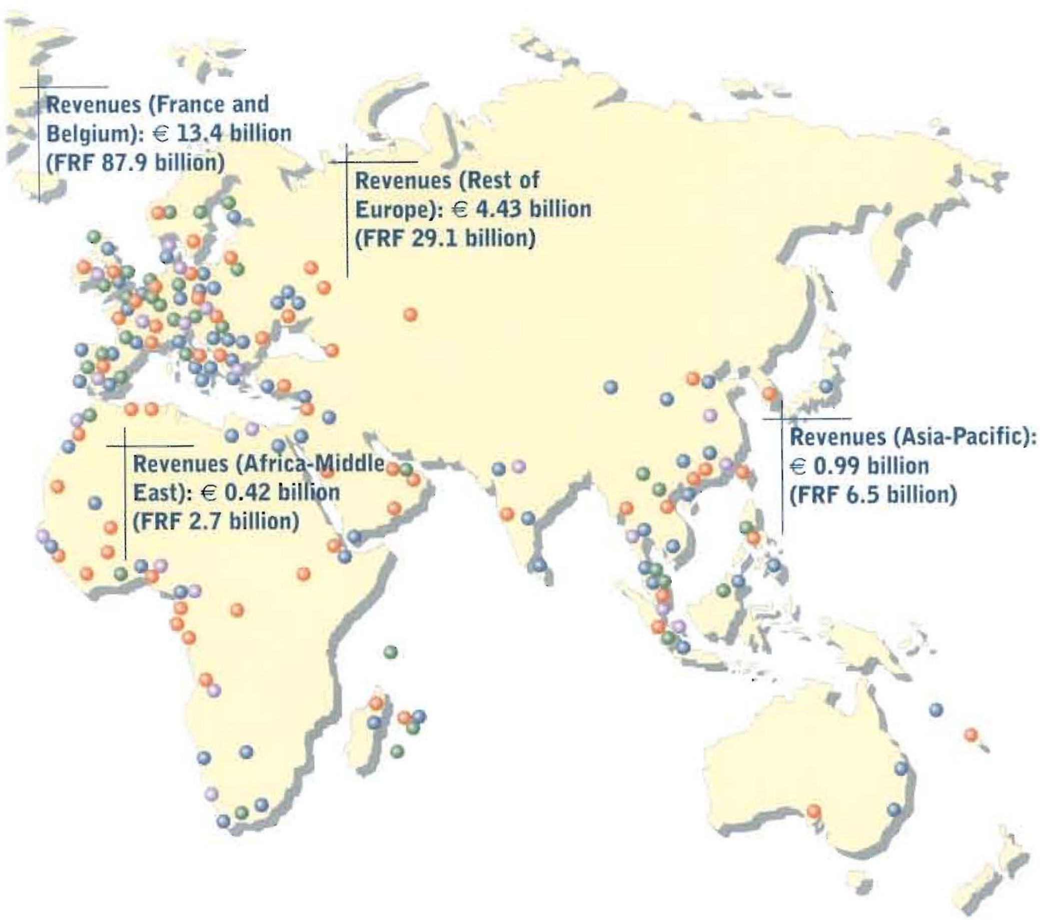
Spain
Waste services (Sita) and Aguas de Barcelona's water companies (Agbar, Lyonnaise des Eaux), water treatment (Degrémont), cogeneration (Elyo), and roadworks (Probisa, Entreprise Jean Lefebvre).

Portugal
Cogeneration (Elyo), water treatment (Degrémont).

Italy
Cogeneration (Tractebel), energy management (Elyo), water treatment (Degrémont).

Hungary
Management of water distribution in Budapest, Pecs and Kaposvar (Lyonnaise des Eaux), building construction (Dumez-GTM), energy production (Tractebel).

S



Czech Republic
Water management and waste water treatment in Brno, Ostrava, and Karlovy Vary (Lyonnaise des Eaux), public works (Entreprise Jean Lefebvre), operation of parking lots (Groupe GTM).

Greece
Construction of the Rion-Antirion in the Straits of Corinth (Dumez-GTM).

Turkey
Water management in Antalya (Lyonnaise des Eaux), water treatment (Degrémont).

The Americas

Argentina
Water management for Buenos Aires and Cordoba, and in the province of Santa Fe (Lyonnaise des Eaux, Agbar), gas distribution in the province of Santa Fe (Tractebel).

Brazil
Energy production (Tractebel), water management in Limeira (Lyonnaise des Eaux), waster services (Sita).

Colombia
Construction and operation of the sewerage plant, Bogota (Lyonnaise des Eaux, Degrémont), water management in Palmira (Lysa).

Venezuela
Construction of high tension power lines (GTMH).

Chile
Energy production (Tractebel).

Mexico
Gas distribution in the Gueretaro region (Tractebel), water management for part of Mexico City (Lyonnaise des Eaux), water treatment for Ciudad Juarez (Degrémont), airport operation (Groupe GTM).

United States
Water management in 14 states, including Indianapolis, Milwaukee and Atlanta (Lyonnaise des Eaux), water treatment (Degrémont), cogeneration and energy management (Tractebel and Elyo), roadworks (Entreprise Jean Lefebvre).

Canada
Operation of the Confederation Bridge (Groupe GTM), construction of a tollroad (Dumez-GTM), roadworks (Entreprise Jean Lefebvre).

Africa

Morocco
Distribution of water and electricity, waste water treatment (Lyonnaise des Eaux, Agbar, Elyo).

Senegal
Water treatment (Degrémont), roadworks (Entreprise Jean Lefebvre).

Nigeria
Assembly of oil platforms and laying of oil pipelines (ETPM), erection of gas infrastructures (Entrepose).

Gabon
Roadworks (Entreprise Jean Lefebvre).

Angola
Assembly and installation of offshore platforms and laying of oil pipelines (ETPM), services to oil companies (GTMH).

South Africa
Supply of drinking water to the provinces of Eastern Cape and Northern Province (Northumbrian), erection of electric power lines (GTMH).

Asia-Pacific

India
Energy production (Tractebel), water treatment (Degrémont).

Kazakhstan
Energy production and distribution, operation of gas transmission lines (Tractebel).

China
Operation of drinking water plants in 5 cities (Lyonnaise des Eaux), construction of hydroelectric structures (Dumez-GTM), waste services in Hong Kong (Sita), water and electricity management in Macao (Lyonnaise des Eaux, Elyo).

Indonesia
Water management for West Jakarta (Lyonnaise des Eaux).

Malaysia
Operation of drinking water plants in 3 cities (Lyonnaise des Eaux).

Philippines
Water management and waste water treatment for Western Manila (Lyonnaise des Eaux).

Singapore
Waste services (Sita), building construction (Dumez-GTM).

Australia and New Zealand
Supply of drinking water to Sydney (Lyonnaise des Eaux), waste services (Sita).

South Pacific
New Caledonia, Vanuatu, Tahiti, Wallis & Futuna: distribution of water and electricity (Ide), waste services (Sita), (Lyonnaise des Eaux, Elyo).

BRIEF GUIDE TO SUEZ-LYONNAISE

Energy

Pages 22 to 27

Tractebel (51%)
Elyo (100%)

Businesses

- Electricity production, transmission and distribution, trading, project engineering
- Gas transmission and distribution
- Facilities operation and maintenance
- District heating and cooling systems
- Heat production
- Cogeneration
- Waste-to-energy

Water

Pages 28 to 33

Lyonnaise des Eaux
Degrémont (100%)

Businesses

- Water management and treatment
- Water treatment process engineering

Waste services

Pages 34 to 39

Sita (51%)
Tractebel*

Businesses

- Collection, sorting, recycling, treatment, bio recycling , waste-to-energy production, and storage of household and industrial waste
- Municipal and industrial waste services

Communications

Pages 40 to 45

Lyonnaise Câble (77%) **M6** (34%)
TPS (25% direct interest and 25% via M6)

Businesses

- Terrestrial TV broadcasting
- Digital satellite broadcasting
- Multiservices on cable
- TV shopping
- Sales of derivative products

Concession management, construction

Pages 46 to 49

Groupe GTM (50%) Cofiroute, Les Parcs GTM, Dumez-GTM, Entreprise Jean Lefebvre, ETPM, GTMH, Entrepose

Businesses

- Concessionary operation of tollroads, bridges, car parks, airports)
- Construction and public works
- Roads
- Industrial construction and contracting

Financial and industrial activities

Pages 52 to 53

Fortis B* (22%) **Union Minière** (25%)
Recticel (70%) **Coficem/Sagem** (20%)
Suez Industrie (100 %)

Businesses

- Savings products
- Life insurance
- Development capital
- Non-ferrous metals
- Polyurethane foam

* 99.41% control via the Société Générale de Belgique Group

DES EAUX BUSINESS SECTORS

Key facts and figures

- **10.77** billion euro (FRF 70.6 billion) in revenues in 1998
- **No. 1** private-sector electricity producer in Europe
- **No. 3** private-sector energy producer worldwide
- More than **40,000** MW of electricity and **103** billion cm^3 of gas supplied worldwide

Strategy

- Double revenues between 1997 and 2002
- Rank among the world's top international independent cogeneration operators and electricity distributors
- Develop electricity and gas systems in Europe, Latin America, and the United States
- Prepare to take advantage of the European trend to deregulation, and take advantage of electricity-gas convergence thanks through its unified division based in Belgium
- Develop integrated multiservices projects (cogeneration, electricity/gas) and outsourcing)

Key facts and figures

- **5.12** billion euro (FRF 33.6 billion) in revenues in 1998
- **No. 1** international player in water-related businesses
- Supplying drinking water to **77** million people worldwide
- Supplying waste water services to **52** million people worldwide
- Drinking water plants and sewerage plants in more than **100** countries

Strategy

- Double revenues between 1997 and 2002
- Consolidate world leadership in water management
  - control resources and entire water cycle;
  - delegated management services in major cities;
  - water treatment technologies
- Our markets: developed and emerging countries
  - development vehicles: Northumbrian Water Group, Agbar, United Water Services
  - major references: Buenos Aires, Casablanca, etc.

Key facts and figures

- **5.12** billion euro (FRF 33.6 billion) in revenues in 1998
- Leader in waste services in Europe, Latin America and Asia

Strategy

- Double revenues and net earnings per share between 1997 and 2002
- Enter attractive markets to give the Group critical mass and a strong competitive position
- Strengthen European leadership and continue to expand in a small number of emerging countries with strong growth (Asia and Latin America)

Key facts and figures

- **0.41** billion euro (FRF 2.7 billion) in revenues in 1998
- **No. 1** cable operator in France
- 13.5% audience share for **M6** in France
- More than 700,000 **TPS** subscribers

Strategy

- Become leading provider of digital multiservices on cable
- Build on success of M6
- Successfully develop TPS

and industrial contracting

Key facts and figures

- **6.88** billion euro (FRF 45.1 billion) in revenues in 1998
- A worldwide presence

Strategy

- Increase share of international operations
- Balance business portfolio
- Develop concessionary management activities, roads, and industrial and electrical contracting activities

Key facts and figures

- **3.06** billion euro (FRF 20.1 billion) in revenues in 1998

No. 1
private electricity producer **in Europe**

No. 3 private sector producer of energy **worldwide**

1999, FORMATION OF A UNIFIED ENERGY DIVISION CENTRED ON TRACTEBEL, TO BUILD A WORLD-CLASS ENERGY BUSINESS

40,000
MW installed, of which 22,000 outside France and Belgium

103 billion cm^3 of gas transmitted each year

10.77 billion euro (FRF 70.6 billion) in revenues (+ 10.3 percent from 1997)

Energy

In the space of just a few years, the energy market has experienced no less than a technological and legislative revolution. The United States and Europe have thrown open their gas and electricity markets. New businesses have emerged, and new players have entered the production, transportation and distribution sectors. Public monopolies have been privatized. Environmental constraints have become tougher. Altogether, these conditions are promoting the emergence of major global players, and Suez Lyonnaise des Eaux has decided to move fast to establish a front-rank international position, in order to seize the opportunities afforded by deregulation.

The single energy sector centred on around Tractebel has set out to become one of the world's foremost players in the main electricity and gas systems (in Europe, the United States, and Latin America).
Energy is the Group's main line of business, and through Tractebel and Elyo, the Suez Lyonnaise des Eaux Group spans every segment of the energy business: electricity production, transmission and distribution; gas trading, project engineering, transmission and distribution; operation and maintenance of facilities; district heating and cooling systems; heat production; cogeneration; and waste-to-energy.

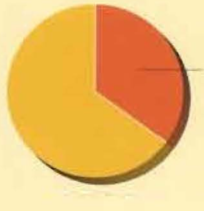
"Monet introduced into painting a vision of light so violent that all forms are dissolved in it. We can now experience this liberation without having to display the same asceticism."
Camille Bryen

KEY FIGURES

in billion	1998 FRF	1998 Euro	1997 FRF	1997 Euro
Contribution of energy sector to consolidated revenues	70.6	10.77	64	9.76
Contribution of energy sector to Group net current income	1.3	0.19	0.9	0.13

ENERGY, THE GROUP'S MAIN LINE OF BUSINESS
(contribution of energy sector to consolidated revenues)

Energy accounts for 1/3 of total revenues



ENERGY Tractebel

JEAN-PIERRE HANSEN
CHAIRMAN OF THE EXECUTIVE COMMITTEE, TRACTEBEL AND EXECUTIVE DIRECTOR

"We are entering a period when it is important to be a significant player in the major electricity and gas systems. Tractebel is one of those, on the world scene."

Tractebel is a global power and services company. Its core businesses are electricity and gas, through Electrabel and Distrigaz in Belgium, and in the rest of the world. As an integrated company, Tractebel is able to supply directly bundled services combining project engineering, technical installations, waste management, and communications. Revenues totaled 11.07 billion euro (Belgian francs 446.68 billion) in 1998.

A key competitive advantage through mastery of electricity and gas technologies

Energy in all its forms plays a vital role in industrial processes, lighting, heating, and transportation.

Tractebel's energy activities cover the production, transportation and distribution of electricity, the transportation and distribution of gas, and energy trading. The company operates a multi-fuel electricity production capacity of more than 37,000 MW, serving customers all over the world. The Group also operates a gas transmission capacity exceeding 100 billion cubic meters per year.

Tractebel is a highly efficient electricity producer thanks to its expertise in natural gas, currently the most economical fuel, while respecting the environment. The combination of electricity with gas gives Tractebel a key competitive advantage.

Market deregulation is creating new opportunities to develop our electricity and gas businesses

With market liberalization and the virtual demise of the concept of national frontiers, power is increasingly a worldwide business. Tractebel has actively prepared for this market opening and is already a front-rank player.

In Belgium, the Government adopted in December 1998 the bill to transpose the electricity liberalization directive into Belgian law. Having anticipated the liberalization of the Belgian electricity market, Electrabel is now poised to play a prominent role on the new European electricity scene. It has continued to overhaul in depth and develop its production facilities. In particular Electrabel has modernized both conventional and nuclear power stations, signed several cogeneration contracts with major industrial customers, completed the Saint-Ghislain Gas-Steam Turbine power station and the contract to build and operate a 350 MW Gas-Steam Turbine power station, both of them in Luxembourg. Electrabel has

A WORLD ENERGY MARKET PLAYER

OUR STRENGTHS:

- **Expertise in all areas of the energy business, from production and transportation to distribution and trading.**
- **Growth in multiservice projects: electricity, gas, heating, cooling, operation and maintenance.**
- **Expertise in the highly complementary electricity and gas markets.**

also embarked on a wide-ranging and intensive program to improve service to both industrial and domestic customers.

In Scandinavia, Tractebel and Electrabel have acquired the energy trading company Scandic Energy, in order to profit from Sweden's and Norway's pioneering experience in the fields of physical and paper energy swaps.

The Belgian cabinet approved the white paper preparatory to liberalization of the gas market in January 1999.

The Interconnector entered service beneath the North Sea, in 1998, with the capacity to transmit 20 billion cubic meters annually between Bacton in England and Zeebrugge in Belgium. This gas is then transported by Distrigaz towards the Netherlands, Germany, and France. Distrigaz continued to enlarge its network in order to handle these large volumes of gas. In particular, it completed the RTR project in record time, and laid 300 kilometers of new pipelines. This project will consolidate Belgium's position on the gas transportation market.

The inauguration of the Interconnector has created new trading opportunities between the UK and continental European markets. Distrigaz has raised its shareholding in the Interconnector from 5 to 10 percent, and begun arbitraging between prices on the UK spot market and on the Belgian market.

On the eve of gas market liberalization, Distrigaz has the know-how and strategic location (Belgium stands at the crossroads of Europe's gas trade routes) to expand its opportunity trading activities in Europe. It is already active as a gas merchant or trader on the Luxembourg and Spanish markets.

Rapid international expansion

Tractebel has developed new projects and acquired existing electricity and gas activities in 22 countries throughout the world. Already its portfolio of international power activities greatly exceeds Tractebel's Belgian businesses, representing 22,000 MW of electricity production capacity, nearly half of it wholly-owned, and 73 billion cubic meters per year of gas transportation capacity over several thousand kilometers.

Tractebel is now the third-largest independent producer of electricity in the world on the global electricity and gas market.

Several major contracts were won in 1998 and early 1999, mainly in Brazil, but also in the United States, Canada, Mexico, and Singapore.

The acquisition of Gerasul, southern Brazil's largest electricity producer, crowned long years of efforts in that country. With a total production capacity of nearly 4,800 MW, Gerasul is strategically located in one of Brazil's most dynamic regions, close to interconnections with the Bolivia-Brazil pipeline and the Argentine gas grid. Gerasul serves a population of 25 million.

The Interconnector gas transmission line entered service in 1998, with the capacity to carry 20 billion cubic meters of gas per year under the North Sea, between Bacton in England and Zeebrugge in Belgium.

ENERGY MARKET LIBERALIZATION IN EUROPE

Deregulation has triggered a reorganization of the electricity industry:

- for suppliers, the challenge is to adapt to the segmentation of electricity businesses, developing new areas of expertise such as trading and brokering;
- for customers, the challenge is to purchase the best service at least cost, and to respect the environment.

Energy trading markets have grown up to manage the relative volatility of electricity, notably in comparison with other commodities.
As an electricity and gas operator, Suez Lyonnaise des Eaux enjoys a competitive edge over newcomers which should allow it to consolidate its leadership in the energy businesses.


Laying pipes for the Interconnector.

ENERGY Tractebel

The Cana Brava project, at the interconnection of the two north-east and central-south electricity grids, now under construction, consists of a concession to build and operate a 450 MW hydroelectric power station on the Rio Tocantins, 250 kilometers north of Brasilia. The gap between energy demand and currently available capacity, reflecting this country's potential. Moreover, Brazil's legal structure and recently-instituted regulatory authority provide a measure of guarantee for investors.

The pipeline between Argentina and Chile represents a strategic growth opportunity for the Group in Latin America. Its construction, sometimes at altitudes higher than the summit of Mont Blanc, is a feat of engineering in itself. This pipeline will initially supply electricity power stations at Tocopilla and Colossa in Chile, operated by Electroandina (a subsidiary of Tractebel), and the Edelnor power station. Subsequently, Tractebel is expected to sign contracts to supply gas to Chile's largest copper mines.

Tractebel made a breakthrough in Mexico in 1998 when it won the concession to distribute natural gas in the Querétaro region, approximately 150 kilometers northwest of Mexico City. This concession was awarded under the Mexican government's policy of involving the private sector in developing and intensifying the use of natural gas. Tractebel will build 613 kilometers of new gas transmission lines in compliance with its obligation to extend the existing distribution grid, in order to serve at least 40,000 connections within 5 years. Tractebel will be distributing some 2 million cubic meters of gas per day by the end of that period.

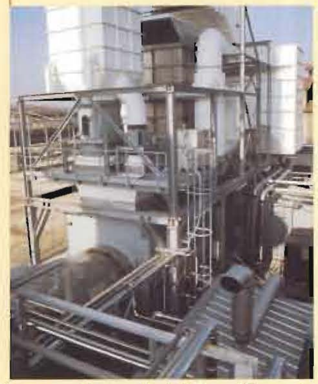
Finally, as planned, work began on the construction and enlargement of power stations at Red Hills (462 MW) in the United States, and Ilo (250 MW) in Peru.

The Nor Andino gas transmission line, one of Tractebel's largest gas projects in the world. This line with supply natural gas from the Argentine gas grid to industrial clients in Chile.

Cogeneration for more efficient energy use

Cogeneration refers to the combined production and utilization of electricity and thermal energy from a single fuel source.
Its advantages are:
- smaller investment outlay; high energy efficiency;
- reliability and simplicity;
- low pollution.

Cogeneration comes in several forms:
- industrial cogeneration: year-round production of electricity and heat to supply continuous industrial demand;
- climate-related cogeneration, associated with district heating systems. These produce electricity and heat during the heating system, depending on the climate;
- dispersed cogeneration: small cogeneration units in office buildings, hospitals, university campuses, and residential buildings.



Cogeneration unit at Solvay (France).

Energy
Elyo

Michel Bleitrach
Chairman and CEO
of Elyo

"Our technical expertise, our experience in the field of power services, and our capacity to design and execute complex operations are our strongest assets in responding to the new challenges in this market, i.e. deregulation, outsourcing, and environmental protection."

As a specialist in rational energy management, Elyo's expertise covers the production of power and services, including cogeneration, district heating and cooling systems, waste-to-energy, electricity distribution and associated production, and operation and maintenance.

Elyo's revenues rose 18 percent over the previous year to more than 2.04 billion euro (FRF 13.3 billion). It now generates nearly 35 percent of this figure outside France, compared with 26 percent in 1997. Elyo undertook a series of structural changes in 1998.

Elyo strengthens its French and European organization

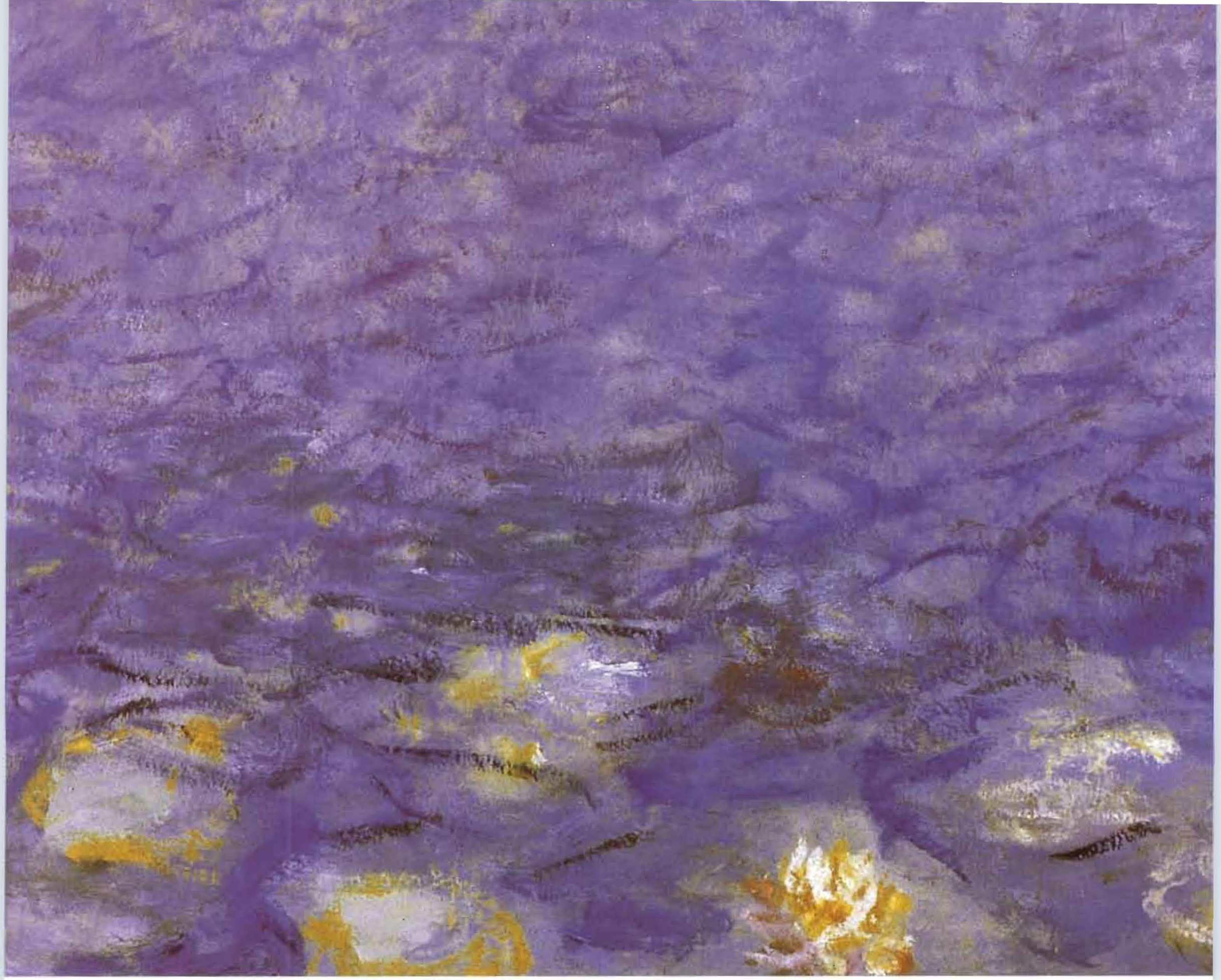
In France, Elyo reorganized by eliminating two of its subsidiaries and introducing a resolutely customer-driven structure at the regional level and at headquarters. The result has been to create a more coherent, effective organization. After delisting Elyo from the Paris stock exchange, Suez Lyonnaise des Eaux carried out a capital increase of approximately 0.30 billion euro (FRF 2 billion). Elyo has expanded its European network to take advantage of the new opportunities opening up as a result of energy market, setting up Elyo Polska in Warsaw and taking a majority stake in its Italian (Petrol Company) and German (Schmeink & Cofreth) subsidiaries.

New industrial contracts signed

Elyo registered especially strong gains in the industrial sector in 1998. It is range of operations included multi-technical and multiservice contracts (for the Astilleros shipyards in Spain, Shell at Berre and the Atomic Energy Centre in Reims, both in France), supplying industrial fluids to Chamatex, high-technology factories (for Saft in Bordeaux), and, above all, cogeneration projects.

Clean, smart power

Two techniques in particular forged ahead in 1998, namely cogeneration and waste-to-energy, thanks to their capacity to combine optimum energy use with environmental protection. Total new cogeneration contracts won in Europe in 1998 represented more than 700 MW of electricity. In the United States, Trigen won new contracts in addition to the 400 MW already in operation. Several cogeneration units were started up 1998, namely: Grays Ferry (225 MW) in Philadelphia; Whitehall in the centre of London; Climaespaço in Lisbon; and Solvay in Northeastern France. Elyo transferred all of its French waste processing and waste-to-energy activities to Novergie (a subsidiary held jointly with Sita). Following this operation, Novergie will now treat more than 4.5 million tons of household waste a year, making it Europe's number one operator in this sphere.
Three new plants designed to the toughest environmental standards entered service in 1998, i.e. Astria (215,000 tons a year) in Bordeaux; Azalys (115,000 tons) in Saint-Germain-en-Laye; and Orisane (110,000 tons) in Chartres.



World
Leader in
water management
businesses

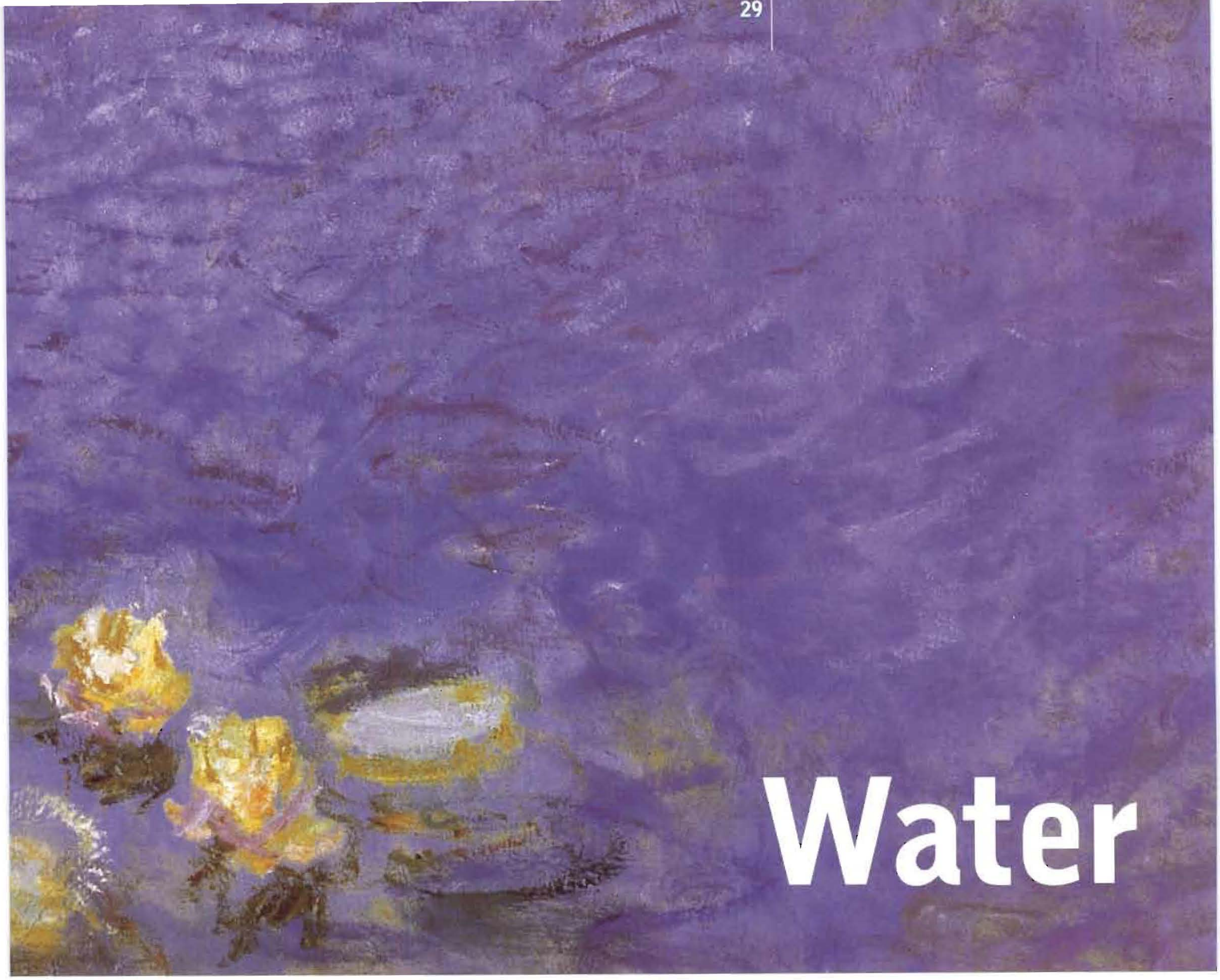
77 million people
supplied with
drinking water

Revenues
5.12 billion euro
(FRF 33.6 billion)

52 million supplied
with wastewater
services

8 MILLION NEW CUSTOMERS IN 1998

A REPUTATION FOR KNOW-HOW SINCE 1880



Water

All the signs are that access to water and its management will be one of the key issues of the new millennium. As the 21st century dawns, one person in five is not connected to the water mains, and one in three has no sewerage. This is a huge challenge, and private management is increasingly seen as an efficient and durable solution to it. Governments of more than 80 countries attending World Conference on Water and development, in Paris in March 1998, stressed the need to draw on the know-how of large private corporations.
In this growing worldwide market for water, Suez Lyonnaise des Eaux consolidated its world water management leadership.
It gained 8 million new customers, and in North American, notably, it now most of the calls for tender the Group entered.

"In painting water, Monet indirectly paints what we cannot see. He addresses that almost-invisible and spiritual surface that separates light from its reflection. The airy azure is the captive of the liquid azure."
Paul Claudel

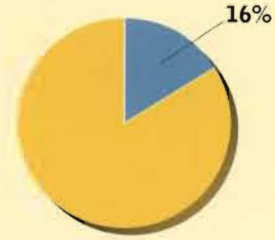
KEY FIGURES

in billion	1998 FRF	1998 Euro	1997 FRF	1997 Euro
Contribution of energy sector to consolidated revenues	33.6	5.12	31	4.73
Contribution of energy sector to Group net current income	1.4	0.21	1.4	0.21

WATER ACCOUNTS FOR 1/3 OF TOTAL REVENUES

(contribution of water sector to Group revenues)

Sustained activity in the developed and emerging countries



WATER
Lyonnaise des Eaux

GÉRARD PAYEN
EXECUTIVE VICE PRESIDENT, WATER

"A public service must serve everyone, or it is not a public service. Lyonnaise des Eaux has harnessed all of its know-how and energy to provide a quality service to the poorest sections of the community, with the acknowledgement and support of the World Bank."

BERNARD GUIRKINGER
SENIOR VICE PRESIDENT-FRANCE

THIERRY BOURBIÉ
SENIOR VICE PRESIDENT-INTERNATIONAL

Competitive technology and a reputation for research and development enabled Lyonnaise des Eaux to retain its leadership, supplying drinking water to more than 77 million people, and 52 million with water treatment services worldwide. Satisfying our customers in Buenos Aires, Indianapolis, Casablanca, Bordeaux, Sydney or Manila is the best guarantee we can offer Lyonnaise des Eaux's new customers in Atlanta, Tuscany, Amman, or Ho Chi Minh City.

Continuing international expansion, and a good start to new contracts

Sales rose 14 percent to 4.9 billion euro (FRF 32 billion) in 1998, as Lyonnaise des Eaux continued to execute its contracts to the highest standards. It also scored several major new successes, especially in the highly promising United States market. This sector made a consolidated contribution of 212 million euro (FRF 1.4 billion) to Group net income, slightly above the 1997 figure. The contribution was split between France (50 million euro/ FRF 329 million) and the rest of the world (162 million euro/ FRF 1.06 billion).

New contracts begun since 1998 contributed to revenue growth. Concession contracts inherently entail heavy investment outlays to begin with, which means they often lose money in the early years before generating steadily increased earnings in subsequent years. Start-up losses on many contracts won in 1997 and 1998 were offset by rising earnings on older international contracts.

In France, 1998 sales rose + 1.4 % at 2.07 billion euro (FRF 13.6 billion). Several hundred contracts in France

(1) Clients effectively supplied within the framework of contracts + 5 years.

SUEZ LYONNAISE DES EAUX SERVES 85 MILLION PEOPLE (WATER SUPPLY AND WATER TREATMENT)

REVOLUTION ON A CHIP

Lyonnaise des Eaux and bioMérieux jointly developed a DNA chip to control water quality more accurately. This high-tech chip is faster and cheaper than existing techniques, combining molecular biology, electronics, chemistry, image analysis and bio-informatics. For consumers, that means better-quality water.

NEW contracts

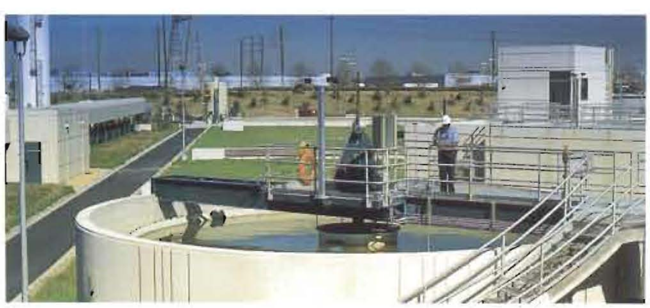
come up for renewal by competitive tender each year, and Lyonnaise des Eaux renewed 173 of its contracts, winning 17 and losing 14. Lyonnaise des Eaux compensated for falling water consumption via a combination of sound management of its contract portfolio and increased provision of services. An economy drive also helped to maintain profitability. As part of the process of introducing a shorter working week, negotiations are in progress with staff representatives and labor unions aimed at boosting efficiency and improving customer service. The division will also continue to seek productivity gains in the years to come. Water operations in France contributed 50 million euro (FRF 329 million) to Lyonnaise des Eaux income, up 10 percent over 1997.

A major storm water management contract was signed with Aéroports de Paris, the Paris airports operator (see box).

Altogether 86 percent of customers expressed satisfaction with Suez Lyonnaise des Eaux's services as a whole in France, while 90 percent of them were satisfied with its customer service. These findings are in line with traditional scores for other public services. Lyonnaise des Eaux is also pursuing an active quality assurance policy, and all of its activities in France will be certified by summer 2000. Currently, more than 80 percent of our operations are certified.

Sales generated outside France increased by 22 percent over the previous year to 2.8 billion euro (FRF 18.4 billion) and now account for 65 percent of Lyonnaise des Eaux's business in terms of sales and 82 percent in terms of population served.

Public/private partnerships to supply drinking water and wastewater services are a fast-growing trend in the United States, where Lyonnaise des Eaux operates under the United Water trade name. Lyonnaise des Eaux has been outstandingly successful on this continent, winning all of the major calls for tenders entered. The most significant contract won was in Atlanta, the largest public/private drinking water supply partnership ever signed in the United States. Other contracts have been won in Milwaukee (Wisconsin), Gary (Indiana), Jersey City, and San Antonio (Texas). Lyonnaise des Eaux now



United Water signed a water treatment contract for Milwaukee (USA).

ENVIRONMENT

Storm water treatment plant at Roissy Charles de Gaulle Airport, for Aéroports de Paris. Paris airports operator Aéroports de Paris awarded the Suez Lyonnaise des Eaux Group a five-year contract to design, build and operate storm water treatment plants for the Paris Roissy airport complex. The consortium members are Lyonnaise des Eaux, Degrémont, Entreprise Jean Lefebvre, Chantiers Moderne, and Safège. Aéroports de Paris has been pursuing an ambitious environmental preservation policy for many years.

Its aim where water is concerned is to treat and clean up environmentally undesirable products such as kerosene, aircraft defrosting and de-icing products spilled onto the runways, or accidental pollution caused by storms or heavy rainfall.

On the strength of three years' experience gained at Orly Airport, Lyonnaise des Eaux is now applying innovative processes to optimize storm water treatment by detecting the onset of storms and heavy rainfall, monitoring water quality, and isolating accidental and chronic sources of pollution. Roissy-Charles-de-Gaulle Airport will be one of very few in the world equipped with a state-of-the-art storm water treatment plant.

(1) Excluding third party accounts in France

THIS WORLD LEADER NEVER STANDS STILL

- Market opening has enabled Lyonnaise des Eaux to win contracts in:
  - Arezzo (Italy), drinking water and water treatment (25 years),
  - Atlanta (USA), production and distribution of drinking water (20 years),
  - Amman (Jordan), drinking water and water treatment (more than 4 years).
- The Group acquired majority control of its companies in Argentina and Indonesia.
- Signature of 2 BOT[1] contracts in China brought the total population served by Lyonnaise des Eaux in that country to 5 million.

[1] BOT: Build, Operate, Transfer.

WATER

Lyonnaise des Eaux

serves 8 million customers in the USA, with revenues of 380 million euro (FRF 2.5 billion).

Several other contracts were signed during the year, including one to manage water supply to 1.5 million inhabitants of the city of Zhongshan in China, a contract to build and operate a major water production plant in Bucharest (Romania), and a waste water treatment plant at Maribor (Slovenia).

A number of important contracts were modified in 1998. Aguas Argentinas, for instance, strengthened its position in Buenos Aires, and the operation will be accretive to earnings per share as from 1999. In Jakarta, Lyonnaise des Eaux raised its stake in the capital of the operating company for the western part of the city from 40 to 100 percent. In the United Kingdom, the water regulator has launched a consultation aimed at cutting the price of water to consumers in April 2000. The actual price cut is expected to be announced in November 1999, but a small number of water companies, including Lyonnaise des Eaux's subsidiary Northumbrian Water, will be authorized to revert to a price above today's level, over a 5-year period.

The water market is currently attracting newcomers, and all players are becoming both more competitive and more numerous. They are becoming more competitive as historical local operators gain experience and bid more keenly in international calls for tender. And their numbers are growing as firms—for the most part American and European—operating in related sectors such as electricity or gas announce plans to use their financial leverage to break into the water market.

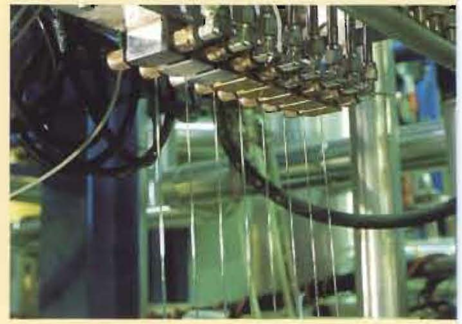
Lyonnaise des Eaux's technical know-how and customer management expertise, together with its reputation and financial muscle, enabled it to win two noteworthy international successes in January 1999. The contract signed in Arezzo (Italy) was the first to be awarded to a private company in the wake of the revision of Italy's legislation governing the management of water supplies. The second contract, in Amman (Jordan), will make Lyonnaise des Eaux a prominent player in the water sector in the Middle East.

Developments in 1999 will consolidate the emergence of public/private partnerships, especially in the United States, Latin America, central and eastern Europe (Germany and Italy). The state of the competition will also become clearer in 1999, as newcomers come under pressure to demonstrate their know-how and profitability over the long term.

Aguas Argentinas is cleaning out the sewers in Buenos Aires.

Know-how and assistance

Suez Lyonnaise des Eaux has developed technically sophisticate in the field of water treatment: pumping water and treating it, transporting it, collecting waste water, treating and depolluting it... all are part of the Group's daily work on 5 continents. That is why in November 1998, seeing the scale of destruction wreaked by Hurricane Mitch in Central America, Suez Lyonnaise des Eaux sent out experts to help these populations in distress, together with emergency water treatment equipment capable of serving 170,000 people.



Manufacturing ultrafiltration membranes.

WATER

Degrémont

Christian Maurin
Chairman and CEO
of Degrémont

"1999 promises to be a very active year on the commercial front. Degrémont plans to venture into new markets such the treatment of sludge derived from waste water: this is a market of the future."

Degrémont is a world leader in water treatment engineering, with sales of 885 million Euro (FRF 5.8 billion) in 1998, an increase of 10 percent over 1997. This increase stemmed from strong growth in conditioning activity and first-time consolidation of the German company Häger + Elsasser acquired in 1998. Net current income came to 10.7 million euro (FRF 70.1 million).

Degrémont gears up for Europe

In 1998, Degrémont embarked on a major project to reorganize and integrate its European network of subsidiaries. This organization will be operational in 2000, enabling the firm to establish closer relationships with its customers and to make the Group's entire Europewide technical, administrative and financial resources available to customers on competitive terms. Degrémont has decided to unify all of its conditioning (chemical water treatment) activities under the name of Aquazur. As Europe's number one chemical water treatment group, Aquazur generated sales of 182.9 million euro and (FRF 1.2 billion) in 1998, representing 20 percent of Degrémont's consolidated sales.

Deploying leading-edge technologies

Particular emphasis was placed in 1998 on developing leading edge technologies in the fields of membrane water treatment and sludge incineration.

The NIRO® fluidized bed incineration technology scored three major successes, in Cincinnati (Ohio) and Northwest Bergen County (New Jersey) in the United States, and a first contract in France, at Elbeuf (near Rouen).

Research into the use of membranes in water treatment has paid off, and the contracts with Lausanne in Switzerland, Del Rio, San Antonio and Glendale in the United States, have established Degrémont's world leadership in the use of ultrafiltration technology to produce drinking water.

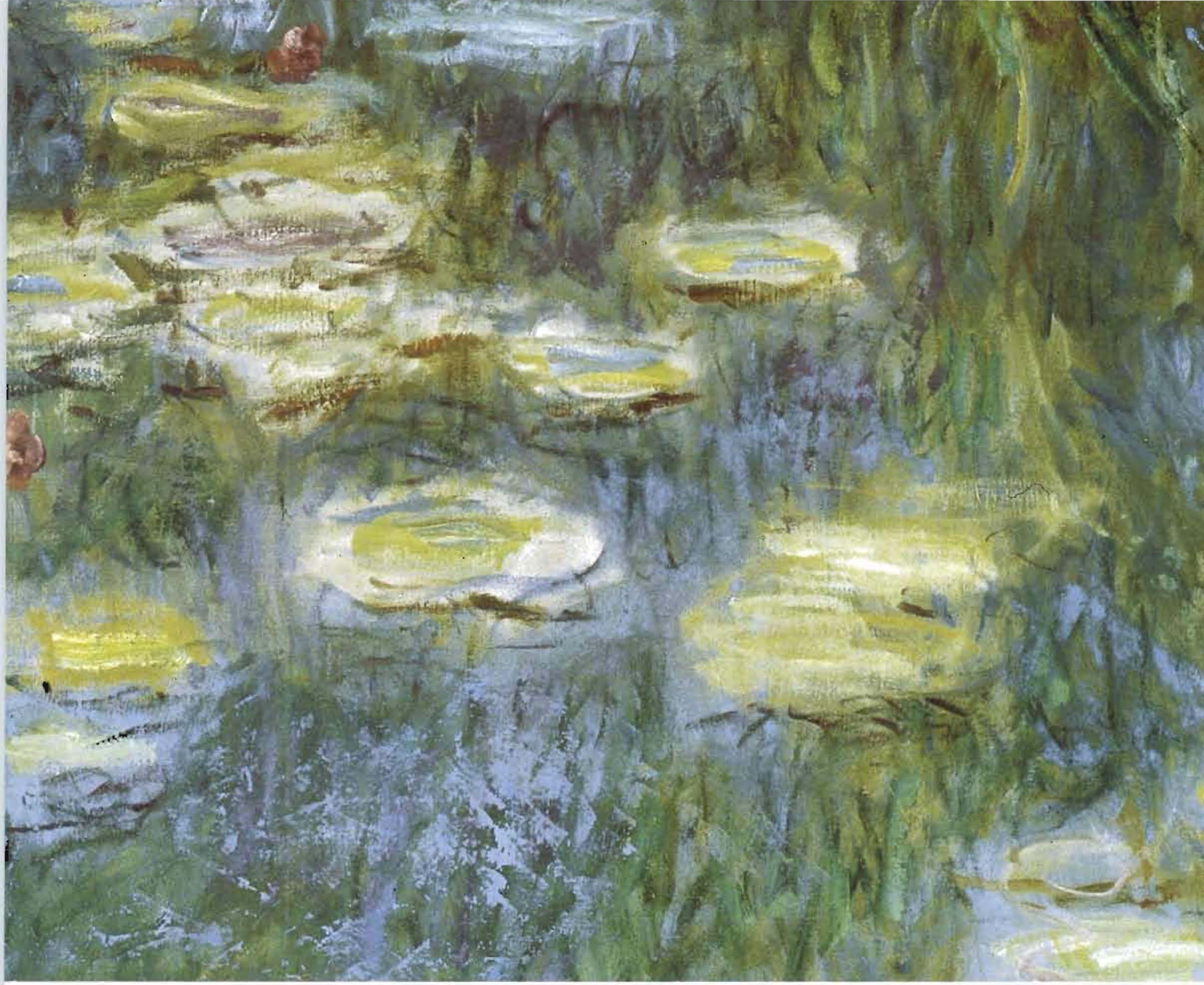
In its drive to offer a full-line service across the water cycle and supply the most up-to-date technologies, Degrémont has broadened its competences with the acquisition of Häger + Elsasser, of Germany, which specializes in the production and treatment of ultra-pure water.

An historic international contract: Cairo

After several years of negotiations, Degrémont won the contract to expand Cairo's waste water treatment plant. This will be the largest unit of its kind in the Middle East and also one of the largest projects in Degrémont's history.

Also in 1998, Degrémont closed three BOT[1] contracts in Mexico, at Ciudad Juarez, Puebla, and Culiacan.

(1) BOT : Build, Operate and Transfer.



Leader
in waste
services

Leader
in Europe,
Latin America
and Asia

Revenues
5.12 billion euro
(FRF 33.6 billion)

ONE OF THE CHALLENGES
AT THE HEART OF SUEZ LYONNAISE
DES EAUX IS TO PRESERVE
AND SAFEGUARD THE ENVIRONMENT.

Waste services

"Monet painted the universe in action, as it grapples within itself (...), from which will arise the enchanting flowers of spring, in preparation for the unfathomable depths of eternal renewal."
Georges Clémenceau

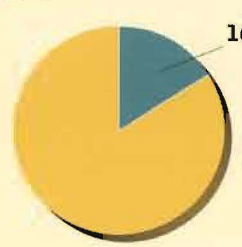
Tougher environmental regulation, market deregulation, privatization: the waste services industry is in the throes of unprecedented upheavals, and growth prospects are strong. For Suez Lyonnaise des Eaux, 1998 brought a change of scale. The acquisition of the international business of US waste operator Browning Ferris Industries (BFI) has made the Group the market leader in Europe, Latin America, and Asia. Its critical mass, global position, expertise and know-how give it the strength to seize the opportunities now arising. The Group's two priorities are to bolster its leadership and pursue its international development.

KEY FIGURES

in billion	1998 FRF	1998 Euros	1997 FRF	1997 Euros
Contribution of waste services sector to consolidated revenues	33.6	5.2	22.7	3.46
Contribution of waste services sector to Group net current income	0.4	0.06	0.4	0.05

CONTRIBUTION OF WASTE SERVICES SECTOR TO CONSOLIDATED REVENUES

Revenues increased by 46 percent between 1997 and 1998



WASTE SERVICES
Sita

JACQUES PÉTRY
CHAIRMAN AND CEO OF SITA

“ The acquisition of BFI's non-North American activities will be accretive to Sita as from 1999. This move marks a turning point for Sita, allowing us to consolidate our front-rank positions in France, Spain, Great Britain, the Netherlands, and Germany. ”

Sita is now Europe's leading provider of waste services, and world number three, following the acquisition of Browning-Ferris Industries non-American assets at the beginning of 1998. Business operations were satisfactory in 1998, with an increase in the number of inhabitants served from 27 million to 40 million as a result of the group's change of size. Revenues, meanwhile, rose 59.4 percent to 2.65 billion euro (FRF 17.4 billion), and operating income was up 84.2 percent to 214 million euro (FRF 1.41 billion). Following the advent of the single currency and harmonization of economic and environmental regulations, Europe is Sita's domestic market, accounting for 85 percent of its total sales.

The large-scale restructuring made necessary by the expansion of Sita's operations was carried out successfully in less than a year. Among the most significant developments were the formation of Sita France and the implementation of synergy with BFI's teams in Britain and Spain, enabling the company to achieve its productivity and cost-cutting targets.

A major european company is born

BFI holds leadership positions in France, Great Britain and Spain, and the acquisition of its non-American assets has enabled Sita to achieve critical mass from a standing start in Germany and Netherlands, two countries from which it was previously absent. In keeping with its policy of teaming up with local partners, Sita is now operating in Germany alongside the OTTO Group, and with Northumbrian Water Group in the United Kingdom, having previously formed an alliance with Aguas de Barcelona (AGBAR) in Spain. In addition to its existing operations in Sweden, Italy, and Portugal, moreover, Sita established new bases for development in Finland and Switzerland.

In France, the key event of 1998 was the formation of Sita France. This is a main subsidiary of Sita, on a par with those in Great Britain, Germany, the Netherlands and Spain, and it has assembled all of Sita's French operations with the exception of hazardous industrial waste treatment, and cleaning. Restructuring projects completed during the year included the reorganization of France Déchets (a subsidiary specialized in Class I or hazardous waste storage), changes in the Group's provincial organization, the transformation of Novergie

[1] Class I: Hazardous waste

Sita operates one of the world's largest storage sites, the Nent landfill in Hong Kong.

(a 50/50 joint- subsidiary held with Elyo, specializing in waste-to-energy) into a network of regional agencies. The 11 Ile-de-France subsidiaries have been combined into a single unit as part of the wider reorganization of Sita's operations in France. Sita France has also begun to overhaul its information systems, with a view to having a modern, effective IT system in place by mid-2000 in order to support the Group's ongoing development. Finally, in January 1999, Sita, Sita France and Sita Déchets were brought together in a new headquarters building in the La Défense business district of Paris.

With sales of 1.1 billion euro (FRF 7.5 billion), up 11.2 percent, Sita France is Sita's largest subsidiary, accounting for more than 43 percent of total revenues. Several major contracts were renewed, including contracts for the collection and/or treatment of household waste in Poitiers, Narbonne, Créteil, and the Chartres District. The 255,000 tons-a-year Astria incineration plant entered service in Bordeaux. The company expanded its services to industry, winning contracts in 1998 to serve the Ford plants in Bordeaux and Charleville, and renewal of the global waste-management contract for the Peugeot plant at Poissy. Finally, efforts to reconstitute the company's waste storage capacity led to the classification of a number of landfill extensions and the creation of "technical waste storage centers."

In Great Britain, synergy between Sita.GB and BFI has yielded savings of 5.2 million euro (GBP 3.5 million): the operations have been reclassified into four categories (municipal services, industrial and commercial waste, landfills and quarries, and incineration). Moreover, the merger in December 1998 of the waste services of Northumbrian Environment Management (NEM), a subsidiary of Northumbrian Water Group (NWG), with those of Sita. Holding UK, confirmed Sita's waste services market leadership in the United Kingdom. The celebration of Sita GB's tenth anniversary in the presence of the UK Minister for the Environment was evidence of how successfully Sita has established itself in Britain. In 1998, Sita. Holding UK's sales increased by 59.7 percent to 412 million euro (FRF 2.7 million).

Among major contracts, the waste collection contract in Bristol was extended for a further two years. The Edmonton incinerator (in partnership with North London Waste Authority) won authorization to incinerate hospital waste.

In Spain, Sita's and Agbar's joint subsidiary, Cespa, wasted no time incorporating the assets of BFI Iberica and taking in hand the day-to-day management and harmonization of services from April onwards. Cespa is now the market leader in hospital waste, having acquired 80 percent of the capital of Athisa (which specializes in the collection and elimination of healthcare waste). Cespa's sales grew by

Sita, a force for a "greener" world

Sita's strong commitment to the environment is making it a leading player in Europe's emerging "green" economy. Its Environmental Report describes the most significant measures taken in this respect, including its sustained research and development effort, the publication of an environmental charter, and above all steps taken in anticipation of European directives on landfills and incineration. By acting even before the promulgation of Europe's environmental directives (which include provisions for the post-operation treatment of landfills, and for the treatment of dioxin emissions), Sita is clearly determined to incorporate environmental issues into its day-to-day commercial and technical activities.

HOW TECHNOLOGY IS SERVING THE ENVIRONMENT

Growing awareness of the need for environmental, on the part of central and local governments, has prompted tough regulation. It has also spawned new waste treatment processes utilizing leading edge technologies.These include recycling, biomass, waste-to-energy recovery, and landfills. The Group notably operates storage centers for ordinary waste equipped with modern discharge-treatment systems, including membrane bioreactors. Through its Research and Development plan, Suez Lyonnaise des Eaux is striving to develop new technologies to prevent the migration of pollutants into the natural milieu (water, ground, air).
Key innovations in landfill management include techniques for preserving groundwater and surface water, and for cutting emissions of greenhouse gases into the atmosphere.

WASTE SERVICES
Sita

57.3 percent in 1998 to 119 million euro (FRF 780 million).
Several contracts were won, renewed, or extended in 1998. These included a 5-year contract to clean new subway stations in Madrid, a 2-year contract to clean parks and gardens in Valladolid, and waste collection and cleaning in Alcobendas.

Sita achieved critical mass from day one in Germany, via OED, a 50/50 joint venture with OTTO, a German waste services provider. Extensive restructuring is now in progress, to streamline and adapt the existing organization to impending changes in corporate taxation and environmental regulation. Sales totaled 199 million euro (FRF 1.3 billion) in 1998.
The primary objective in the Netherlands is to put new management structures in place and reorganize sales activities. A number of new municipal and industrial contracts were won in 1998, including those for Citroën Nederland and Philips Lighting. Sita BV generated sales of 174 million (FRF 1.1 billion) in 1998.

Wide-ranging international ambitions

Sita has been an operator in Brazil since 1997, through its subsidiary Vega Engenharia Ambiental (VEA). Revenues in 1998 came to 222 million (FRF 1.5 billion), thanks to a series of new contracts and renewals. These included a composting unit for the city of São Paulo, and waste collection for the cities of Campo Grande and Barra Mansa. Sita is also present in Peru and Argentina.
In Hong Kong, Sita has acquired 30 percent of the Swire-BFI joint venture, with the Hong Kong government's approval, the BFI assets having been incorporated into the new Swire-Sita unit. Revenues totaled 81 million (FRF 532 million) in 1998. The Hong Kong authorities are considering privatizing household waste collection, and Swire-Sita responded to several calls for tenders in the third quarter of the year. Swire-Sita also started operation of the Went site's leachate treatment unit, and is progressively opening 8 transfer stations.

ACKNOWLEDGED EXPERTISE IN THE TREATMENT OF SPECIAL WASTE

TERIS, a joint 50/50 subsidiary of Sita and Rhodia specializing in the treatment of hazardous waste, this year reorganized its businesses into 4 coherent lines, i.e. SCORI (pre-treatment and cement industry waste in France); TERIS (complex waste), to which another company, Labo Services, has been attached; a European division (covering Spain and Belgium); and an Overseas division (Brazil, Korea, and Australia). A vigorous sales drive generated revenues of 69 million (FRF 456 million). This units is a world leader in its sector and expects to achieve strong growth in 1999.

THE WASTE SERVICES MARKET: A MARKET WITH A FUTURE

Suez Lyonnaise des Eaux is a major operator in the fast-expanding household and industrial waste services businesses.
Key market data:
- 30 billion euro in Europe (FRF 200 billion)
- 30 billion euro in United States (FRF 200 billion)
- 5 billion euro in Asia (FRF 30 billion)
- 5 billion euro in Latin America (FRF 30 billion).

WASTE SERVICES
Tractebel

Tractebel's know-how in environmental services comprise the integrated management of solid and liquid waste, as the well as the treatment of liquids and sludge. Revenues increased by 30 percent in 1998 to 694 million euro (Belgian francs 28 billion).

A major player in Europe

Tractebel is a major integrated waste services operator in Belgium, and also operates in other countries, notably the United Kingdom, Eastern Europe, and Canada.

Tractebel enjoys a strong reputation for expertise in leading-edge waste recycling and waste-to-energy technologies. These techniques are helping to cut the volume of waste stored in landfills, a major concern among those involved in the waste business.

It has built on its expertise and know-how to expand into the treatment of hazardous waste and remediation of polluted ground in Belgium, France, Germany, and the Netherlands.

New growth prospects

In 1998, Tractebel consolidated its Belgian market leadership in all types of waste. It also further reinforced its already strong position in the Netherlands with the acquisition of three companies, Ecotechniek, Holwarda and Van Bennekom, at the beginning of 1998. The resulting group is thus now one of the largest operators in the sector.

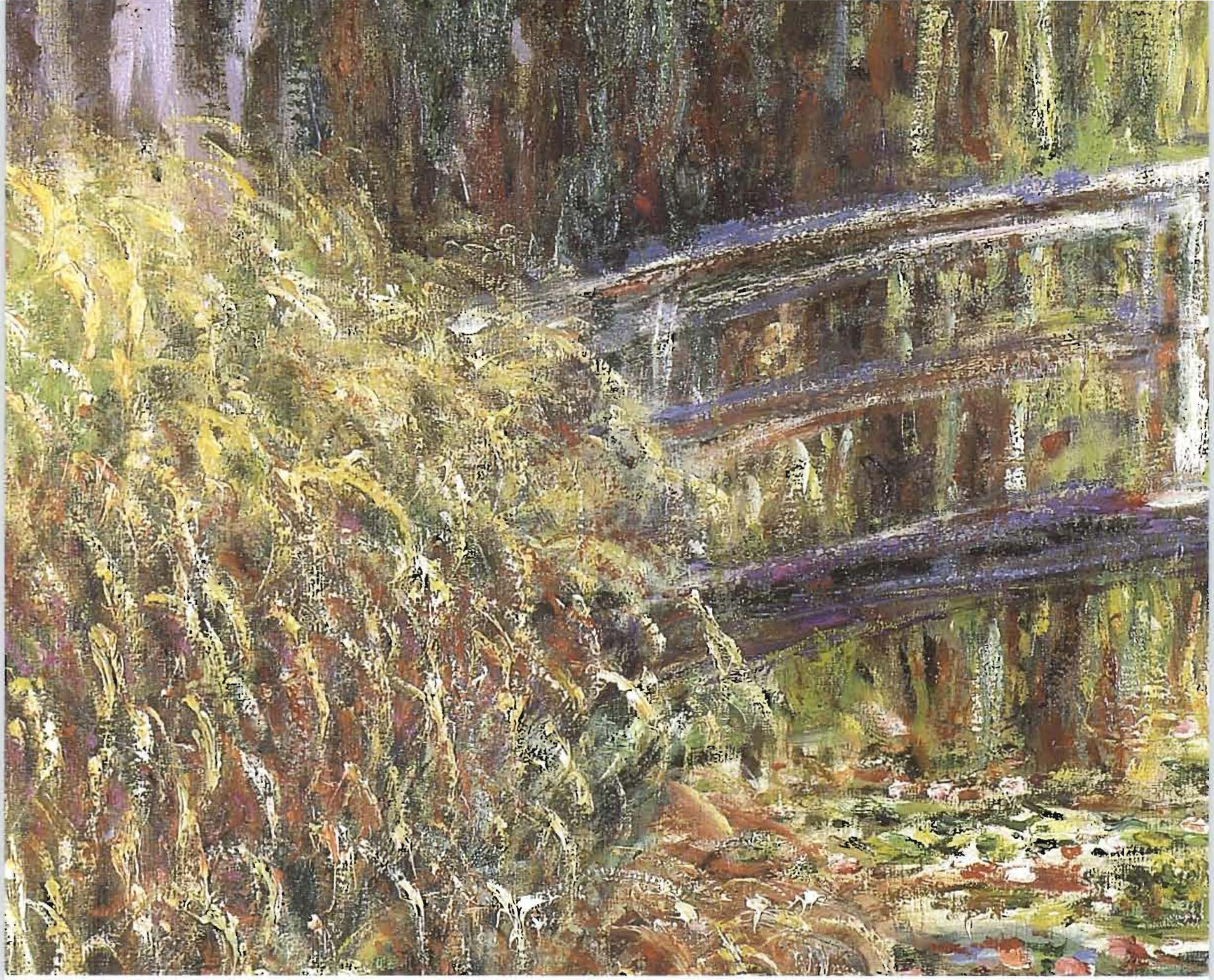
UK operations have grown considerably following the acquisition of Lancashire Waste Services in 1997. In 1998, Tractebel was awarded the integrated waste management contract for the District of Kirklees (Northeast Manchester, 400,000 inhabitants). This project provides for the design, rebuilding, financing and operation of the Huddersfield incinerator.

Tractebel also acquired A & J Bull in August 1998. This important London-based company owns landfill centers and a network of transfer centers throughout Southeast England.

In Poland, Tractebel continued to build up a strong presence in the south and east of the country, serving more than 6.5 million inhabitants. With sales up 40 percent over 1997, it is now one of the three largest private operators.

In Canada (Province of Quebec), Tractebel registered further significant growth, acquiring Transvick and Bessette in Montreal, and AES in Chicoutimi. Here too, Tractebel is now one of the three largest main private operators.

Fabricom waste sorting center.



700,000
Lyonnaise Câble
subscribers, all services combined

700,000
TPS
subscribers

Revenues:
0.41
billion euro (FRF 2.7 billion)

M6
advertising revenues up
14% percent

PART OF THE DIGITAL AND INTERNET REVOLUTION

Communications

The communications market is forecast to double in the next five years, on the back of the generalized deployment of digital broadcasting, the development of new technologies and new Internet-based services, and deregulation. The Group intends to be a multiservice operator in these key business, providing TV, Internet and telephone services over its cable networks (in France and Belgium). It also plans to build on the commercial success of TPS and to amplify that of M6. Suez Lyonnaise des Eaux holds significant positions in two technologies now spearheading the communications revolution, namely:

- cable, where Lyonnaise Câble, with 100,000 digital connections out of a total of 700,000, makes it one of the world's foremost digital cable operators. These can be used to supply a wide range of services to consumers, including digital TV, broadband Internet access, and cable telephone.
- satellite broadcasting, where TPS now supplies a full line of programs and leading-edge technology to its nearly 700,000 subscribers*, for their greater convenience.

M6, meanwhile, is now France's no.2 TV channel by advertising revenues.

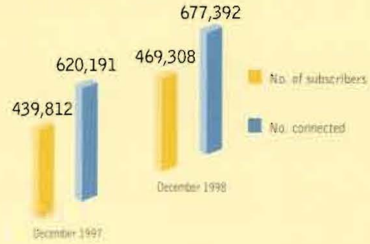
*april 1999

"Monet's mental disposition seems to be that of a great painter who has decided to give himself a field of vision sufficiently vast to embrace the world. A cosmic vision, I should like to say."
André Masson

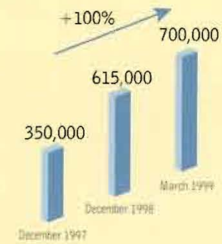
Key figures in billion	1998 FRF	1998 Euro	1997 FRF	1997 Euro
Contribution of communications sector to consolidated revenues	2.7	0.41	2.4	0.37
Contribution of communications sector to Group net current income	(0.2)	(0.03)	(0.1)	(0.02)

Number of subscribers

Lyonnaise Câble



TPS



Communications

Lyonnaise Câble

Alain Hellequin
Chairman and CEO,
Lyonnaise Câble

With 700,000 homes connected (all services combined), the number of Lyonnaise Câble subscribers increased by 7 percent in 1998. France's no. 1 cable operator generated 170 million euro (FRF 1.1 billion) in revenues in 1998. Thanks to its central position on the French market, Lyonnais Câble operates and manages a nationwide network of 25 sites, including Paris, representing 2.5 million potential connections and possible connections for 400,000 professionals and businesses. Since their first experimental multiservice offerings in 1995, these 25 local networks have aggressively developed new interactive services which are accelerating the convergence of audiovisual and telecommunications services.

“ Cable's rebirth in the United States is also taking place in Europe. Lyonnaise Câble anticipated this some years back, maximizing the capacity of its cable networks by developing an all-digital service spanning TV, Internet access and telephone communications. ”

Contributing to the development of a fast-growing market

The advent of digital TV and new technologies are radically transforming the market for telecommunications, information and media services. The market is forecast to double in the next five years.

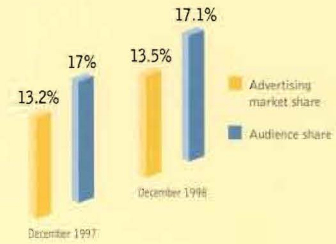
In 1998, the French telecommunications regulator, ART, confirmed the opening up of the local telephone line loop to competition, paving the way for the introduction of new services on cable networks. The ART's ruling entrusted responsibility for maintenance of the Plan Câble networks to Lyonnaise Câble. It also set a precise timetable for the opening up of the Paris network, authorizing the supply of voice services. Telemarketing's steady growth has now established this as the prime channel for the sale of all Lyonnaise Câble products. Also in 1998, Lyonnaise Câble launched a product offering aimed at businesses and professionals.

Ten times more channels with digital technology

The Communications sector received a fresh boost from the roll-out of digital technology in Autumn 1997. The number of channels available has increased tenfold, image and sound quality have improved, and new interactive services have been launched. Lyonnaise Câble has developed a simple yet comprehensive TV service. With just a set-top box, and no need for a satellite dish, subscribers can number receive nearly 100 channels, in French and other languages, including general and special interest channels, movies, the arts, sport, music, youth programs, news and current affairs, documentaries, fashion, weather, etc.

At the same time, new interactive services have been launched. In Autumn 1998, Lyonnaise Câble launched its

M6 AUDIENCE SHARE



PARIS PREMIÈRE

Paris Première broadcasts round the clock to 2,500,000 homes by cable and satellite. It is the leading special-interest channel by peak time audience, broadcasting a blend of shows reflecting the variety of Paris life (arts, fashion, movies, theater, opera, music, literature, comedy, sport, variety shows, etc.).

electronic program guide to help subscribers make their selection. This interactive guide is available at all times to inform viewers of programs now showing or coming up next; it can announce all programs, or just highlights, for the next week; it can classify programs by broad theme, and even give a brief description of eacb program.

This richer program offering and the new interactive services are generating steadily revenue growth per subscriber.

Digital subscribers accounted for nearly 20 percent of all home TV subscribers in 1998.

Broadband Internet access

Cable has the capacity to carry large amounts of data at high speeds, and allows subscribers to remain permanently connected. That makes it an ideal–and the most economical–channel for the distribution of interactive Internet services. Major players in the industry foresee bringing together a TV decoder and cable modem in a single box, permitting the marketing of combined TV and Internet offerings.

Lyonnaise Câble's Internet brand, CyberCâble, is aimed at people wanting a permanent connection, high quality sound and image, high speed data transfer, while leaving their telephone line free. Through its "portal" approach, CyberCâble has signed agreements with content providers and online services, enabling Lyonnaise Câble to offer subscribers a broad range of business and leisure services.

In February 1998, Lyonnaise Câble signed a letter of intent to form a partnership with the French Ministry of Education, Research and Technology to develop Internet access for schools at all grades and places of higher education.

In addition to consumer applications, cable access allows small and medium-sized businesses to connect several PCs to the Internet at once.

Work on upgrading Lyonnaise Câble's Plan Câble networks, which is required in order to deploy voice-image-data services, will be carried out in Paris and the Paris region in conjunction with France Télécom in 1999.

To ensure the maintenance of the Plan Câble network with which it has been entrusted by ART, Lyonnaise Câble is setting up teams on a national level. At the same time, Lyonnaise Câble has expanded its backbone transmission capacity between its different sites, as well as national transmission platforms for national and international link-ups.

Sharpening our customer focus

Lyonnaise Câble is strengthening its organization for better customer service and to increase productivity. A nationwide telephone call center is being set up, and new IT software is being developed to fine-tune the pricing of Internet and telephone services.

In 1999, Lyonnaise Câble intends to ride the wave of digital and Internet services to win over new customers, developing combined services to boost revenue per subscriber.

With the launch of a high-end broadband service for intensive Internet users, Lyonnaise Câble is aiming to attract the professional and SME market, in order to capitalize on that market's exponential growth prospects. 55 percent of professionals are forecast to be connected within 5 years, compared with 5 percent in 1998.

In a fast-growing communications market, Lyonnaise Câble is gearing up to expand its range of services, and is considering a host of technological opportunities. Examples include the cable-telephone service already being marketed in Annecy and Chambéry (Southern France), as well as innovative solutions such as IP (Internet Protocol) voice telephony.

Synergy through partnership

Lyonnaise Câble:
- seeking telephone and Internet partners.
- technical partnerships with Sagem (digital TV), Motorola (Internet), and Alcatel (telephony).

TPS: since its inception, TPS has formed partnerships with:
- French film companies
  - Gaumont
  - Film par Film
  - Hachette Première
  - Ice 3
  - Vertigo),
- Interactive financial services
  - Crédit Agricole,
  - Vega Finance,
  - Les Echos
- Educational multimedia - Lagardère
- Organizations (FNIH—National hotel trade federation).

M6:
- Hachette (Marie-Claire)
- Fun TV
- European channels: Pro Sieben (Germany), Channel 5 (UK).

TPS

Just two years after its arrival on the extremely competitive French TV broadcasting scene, TPS's digital service has attracted numerous subscribers thanks to its varied programming. More than 275 million euro (FRF 1.8 billion) have been invested over the last year. Whilst developing this offer. TPS continues its investment policy in the cinema.

Jacques Espinasse
Chief Executive Officer, TPS

"We are a major contributor to the French film industry. Not including catalogue expenditures, we have already invested more than FRF 300 million. That is a lot of money for a company that started from scratch two years ago, and that now has 700,000 subscribers."

TPS broadened its offering in 1998 with the introduction of 11 new channels: M6 Music, Mezzo, Régions, RFO Sat, Club Téléachat, Shopping Avenue, Infosport, Escales, MTV, BET On Jazz, and M2, together with two optional channels and music channels and sound broadcasting stations. TPS now broadcasts more than 90 channels.

A year of dynamic activity

As a TV broadcasting service resolutely aimed at a very broad public, TPS's programs are broadcast to family audiences. Its public is younger than the national average (under 35), and better-equipped. At mid-1998, 95 percent of subscribers reported they were satisfied with the number of channels available, and 87 percent said they received good value for money. That explains why 95.4 percent of TPS subscribers renewed their subscriptions at the due date (in May 1998).
For even greater viewer comfort, the national general interest channels, TF1, France 2, France 3, and M6 now broadcast their prime time programs in 16/9 wide-screen format. TPS has also launched a new statistical multiplexing broadcasting technology to maintain its French market leadership in terms of pictureand sound quality.
TPS continued to pre-finance French movie productions, signing agreements with Gaumont, Film Par Film, Hachette Première, Ice 3, and Vertigo for the right to show their films on Multivision payper-view channel, and on the Cinestar channels. TPS's movie channels (Cinestar 1 and 2, and Cinétoile) captured a larger audience share than competing movie offerings on cable and satellite TV combined, in the first quarter of 1998.
In sports broadcasting, TPS broadcast all 64 soccer matches during the Football World Cup, including 44 matches in 16/9 wide-screen format (many of them in Dolby Surround) on its Superfoot 98 channel. In July, finally, TPS launched Infosport, the first all-digital continuous sports news channel.

Interactive TV acclaimed

In 1998, TPS and its terrestrial channel shareholders began broadcasting interactive services in addition to their programmes, especially during TV commercials accompanying live sports broadcasts and TV shopping programs. TPS also launched an interactive sports show, Infoscore, and the first fully-interactive financial news channel ("F1 La Chaîne Financière") with three initial partners (Crédit Agricole, Vega Finance, and Les Echos). Another new launch in 1998 was Espace Annonces, a small-ad channel. TPS interactive services scored an 84 percent satisfaction rate among subscribers, and consumer magazines also have hailed the new service.
In 1999, TPS plans to launch a package of educational channels and multimedia services with ("Sat&Clic") in association the Lagardère Group. This offering will be made available to 250 pilot schools in an experimental program being run by the CNES for the French Ministry of Education. TPS will also be developing a new movie channel and other innovative services.
Constant summary of sporting events, interactive publicity devoted to employment, Adecco interactive weather forecast for travellers. With these two poles of development, the cinema and sport, TPS's next target is to reach 1 million subscribers in 2000.

M6 broadcasts more prime time news magazines than any other channel in Europe. In the wake of its successful "Capital" (see photo), M6 has launched "Zone Interdite," "E=M6," "Pourquoi ça marche," "De quel droit," "Mister Biz," and "Les chemins de l'impossible."

COMMUNICATIONS

M6

M6 TV channel gained audience share significantly, rising from 13.2 percent to 13.4 percent, for the eleventh consecutive year. It was the only major national channel in 1998 to gain ground in the under-50 age group, with an average audience share of 17.8 percent. M6 further consolidated its position as the second most popular channel among children and young adults (15-34 age group).

JEAN DRUCKER
CHAIRMAN AND CEO, M6

"Over the past 11 years, we have built up a format aimed specifically at the under-50s. Day after day, we have learned to think, produce, buy and schedule programs by studying our successes and our setbacks. Today we are the only channel to be making such strong gains among the under-50s."

Group revenues totaled 526 million euro (FRF 3.5 billion), with estimated Group income of 61.4 million euro (FRF 403 million), up 29.4 percent. Increased audience ratings translated into a 14 percent growth in advertising revenues, double the rate of growth for the market. In 1998, M6 became the number two French TV channel in terms of advertising spending. Diversified businesses also grew rapidly, with revenues exceeding FRF 1 billion for the first time and contributing 30 percent of consolidated revenues.

M6 is building on its dynamism and sound financial condition to diversify its avenues of growth, despite a high level of investment. Among the latter, it notably increased its equity stake in TPS (from 20 to 25 percent), in TCM (from 33 percent to 41.25 percent) and in HSS (from 66 percent to 100 percent). Two new special interest channels–M6 Music and Club Télé Achat–were launched in 1998, bringing the number of channels developed by M6 to five (the others being Série Club, Teva, and Fun TV).

A subsidiary, M6 Interactions, registered several commercial successes, with 9 million CDs sold, 3.5 million publications (it currently publishes 11 titles). Its first CD-Rom ("E=M6" based on the popular science show of the same name) is one of the best-selling titles outside the games market, while visits to the company web site were up 400 percent.

HSS, M6's TV shopping subsidiary, also recorded strong growth, with sales up 30 percent. It successfully launched a 24-hour TV shopping channel on the TPS satellite TV service, and formed a 50 percent joint venture with TVA, the leading producer of TV shopping programs in Canada.

M6 Droits Audiovisuels is building up its export sales of broadcasting rights. Notable sales have included TV films such as "Combats de femmes" and "Verdict", as well as the news shows "Turbo", "Capital", and "Les Chemins de l'Impossible".

M6: still creating value, holding onto its leadership

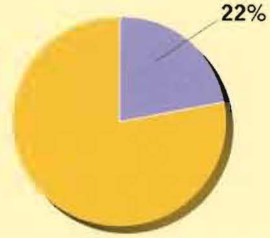
M6 will pursue efforts to broaden its audience in 1999, especially in the 35-49 age group, thanks to imaginative, contemporary programming. It will be strengthening its prime time Tuesday evening news shows, further developing its production of TV films (20 are planned for 1999). As part of its efforts to expand its local news coverage, M6 has applied to the French broadcasting authority for permission to launch local newscasts for the Paris region, Nice, and Clermont-Ferrand.

M6 also intends to bolster its know-how in diversified businesses, preparing for the launch of new special interest channels for TPS (satellite) and cable TV, notably stepping up its investment in multimedia programming. TV shopping channels, meanwhile, will extend their international reach, particularly in Hungary, Argentina, and Canada.

KEY FIGURES

in billion	1998 FRF	1998 Euro	1997 FRF	1997 Euro
Contribution of construction sector to consolidated revenues	45.1	6,88	43.6	6,64
Contribution of construction sector to Group net current income	0.4	0.06	0.3	0.5

CONTRIBUTION OF GROUP GTM TO CONSOLIDATED REVENUES



Groupe GTM

JEAN-LOUIS BRAULT
CHAIRMAN AND CEO
OF GROUPE GTM

"Our 1998 figures confirm the wisdom of our strategy in terms of both revenues and earnings. Groupe GTM is growing significantly and winning some major commercial successes at the same time."

With consolidated revenues of 7.38 billion euro (FRF 48.4 billion), versus 6.88 billion euro (FRF 45 billion) in 1997, Groupe GTM registered further growth both in France and abroad, in 1998. Non-French revenues now account for 43.6 percent of its total business. As part of strategic moves to re-balance its business mix, significant developments took place in roadbuilding, offshore construction and infrastructure concession operations. Conversely, the relative share of construction and public works fell to 35 percent, down from 41 percent in 1997 and 46 percent in 1995.

Several significant contracts were won to manage car parks in France and abroad (in particular for airports in Mexico and tollroads in Canada), in 1998. As forecast, consolidated net income for 1998 came to 65 million euro (FRF 429 million), a significant improvement (+ 69%) on the 1997 figure of 39 million euro (FRF 254 million).

Infrastructure concessions

Groupe GTM continued to expand its infrastructure management business as a member of various consortia in 1998, winning contracts to manage airport facilities, bridges and viaducts, and tollroads.

It began the year with the signature of a 30-year concession contract to manage 200 km of tollroad in Canada, between Fredericton and Moncton. Coming after the opening of the 13-km Confederation Bridge, this new contract further strengthened Groupe GTM's position as a manager of infrastructures in Canada. Traffic on the Confederation Bridge in its first year of operation was in line with forecasts.

The 80,000-seat Stade de France sports stadium outside Paris was inaugurated at the beginning of 1998 and successfully demonstrated its capacity to host major sporting events such as the Football World Cup.

The foundation stone of the Rion-Antirion bridge in Greece, one of the largest infrastructure projects in Europe, was laid in 1998. The bridge will enter service in 2004 and will be managed under a 42-year concession contract starting from the end of 1997.

At the end of the year, Groupe GTM was awarded the concession to operate 9 newly-privatized airports in Mexico (total capacity, 10 million passengers a year).

Two outstanding events in 1998 for Les Parcs GTM, the car park concession operator, were:

- the award, by SAP, of a 20-year concession to operate 7,000 parking spaces in

The Stade de France (Paris) hosted more than 1 million spectators, not including the World Cup, in its first year of operation

built-up and kerbside car parks and in the road, in Saint-Etienne,

- the award of a 25-year farm-out contract to operate the West India Quay car park in London's docklands. Les Parcs GTM already operates the Mayfair car park in London.

In France, operations were buoyed by healthy consumption and a new sales drive, leading to significant revenue growth in line with forecasts.

At the end of 1998, Les Parcs GTM operated 170,000 parking spaces and more than 200 car park buildings in 67 cities in France and other countries.

Roadbuilding

Jean Lefebvre generated 2.06 billion euro (FRF 13.5 billion) in sales in 1998 (+ 12 percent), with international and overseas sales accounting for more than 45 percent of the total.

In addition to healthy demand in France and abroad, 1998 was a year of vigorous external growth, with the acquisition of Blythe in the United States, the signature of a partnership agreement with the Czech firm ODS-DSO, the acquisition of STR-Huys (Northern France), that of Smag quarries in Southeastern France, and the takeover of Saged's roadbuilding and materials trading business in the Paris region.

In the maintenance sector, the GTM's Spanish subsidiary Probisa won a four-year contract to maintain and operate 250 kilometres of highway, while Ringway won two global maintenance contracts in the United Kingdom. All three operations confirmed the Group's determination to develop this type of partnership.

Major contracts won in 1998 included the RN 160 national trunk road in the Indre-et-Loire department, the tramway installation in Montpellier (both in France), the Eastern bypass at Nouméa in New Caledonia, mending of the main runway at Montreal airport, and a new tollroad section in the Czech Republic.

Construction and public works

Dumez-GTM 's sales totaled 2.4 billion euro (FRF 15.8 billion) in 1998. In keeping with GTM Group's strategy, this figure is down by approximately 6 percent relative to 1997. It is split equally between construction and public works, with revenues from outside France representing 39 percent of the total.

In France, the outstanding event of 1998 was the integration of blank Construction's subsidiaries into the regional organization of GTM Construction, thus streamlining the Group's French network, which also comprises Chantiers Modernes and its subsidiaries.

While the construction industry began to pick up, conditions remained difficult in public works, and

New contracts

Several developments in 1998 illustrated GTM's strategy of shifting the balance of its operations toward businesses that generate recurring revenues (infrastructure concessions, roads, industrial and electrical services).

At the same time, it expanded its international reach via a number of moves :

- Entreprise Jean Lefebvre acquired the American road builder Blythe, which operates in North and South Carolina (November 1998),
- A contract to build 14 km (8.75 miles) of tunnels for London's Heathrow Airport extension (July 1998),
- A concession to operate the 540-place London Docks car park (December 1998),
- Construction of a tunnel of more than 3 km (1.8 miles) and the largest viaduct for the future high speed rail link between London and the Channel Tunnel (September 1998),
- After terminating its partnership with McDermott at the beginning of 1998, ETPM, as part of the development of the latter's Girassol fiald in Angola. Total value of contract, 1.07 billion euro (FRF 7 billion), worth 457 million euro (FRF 3 billion) to ETPM

GROWTH IN INFRA-STRUCTURE CONCESSION MANAGEMENT

In december 1998, Groupe GTM, as part of a consortium, won the concession to operate 9 airports in Mexico, as part of the program to privatize the Southeastern Goup of Mexican airports. The airports handles nearly 10 million passengers a year, including 6 milion at Cancun alone

Cancun Airport, Mexico. Goupe GTM is a member of the consortium that operates the 50-year airport concession

GROUPE GTM

sales totalled 1.5 billion euro (FRF 9.8 billion).

Several major projects were completed in 1998, including renovation of the Edouard VII block in Paris, and construction of the France Télévision headquarters in Paris, the water treatment plant at Colombes, and the fourth runway at Roissy Airport. Major orders taken in 1998 include the rehabilitation of the Gaz de France headquarters (22 million euro/FRF 144 million), an earthmoving lot for the A 89 tollroad, and installations for the Roland-Garros tennis complex in Paris.

Outside France, Dumez-GTM generated sales of 470 million euro (FRF 3 billion), including 32 percent in Europe outside France, 33 percent in Asia, particularly in China, 18 percent in North America, and 10 percent in South America. Significant orders booked in 1998 were: construction of the Fredericton-Moncton tollroad in Canada (106 million euro, FRF 695 million) under a concession contract with the GTM Group, tunnels in Hong Kong (60 million euro, FRF 393 million), the tunnel and a viaduct on the high-speed rail link between London and Dover (60 million euro, FRF 393 million), and work on Heathrow airport terminal 5 (80 million euro, FRF 524 million) in the United Kingdom.

Dumez-GTM's main international subsidiaries (CFE in Belgium and Wiemer und Trachte in Germany) kept up their revenues at 470 million euro or FRF 3 billion (Group share).

Industrial Contracting and Services

Entrepose and Delattre-Levivier specialize in pipefitting, boilerworks and mechanical maintenance. Entrpose reported revenues of 580 million euro (FRF 3.8 billion) in 1998, of which 44 percent was generated outside France, mainly in the oil and gas industries. The French agency network currently numbers nearly 140 units. Local works and services contracts saw satisfactory levels of activity, and in particular the network was awarded several multi-year operations and maintenance contracts. In the industrial construction and equipment sector, brisk activity large-scale pipe laying projects notably included the completion of oil pipelines in Libya, the construction of gas transmission lines in the United Kingdom and Canada, and water supply structures in Senegal. Work continued on complex oil and gas structures, notably on a gas compression station in Scotland, in the Middle East, in Nigeria (where it is engaged in extensive rehabilitation of the Kaduna refinery), and in China, where it is under contract to supply ten 10,000 cubic-meter gas storage spheres.

Following the opening of a representative office in Baku (Azerbaijan), in partnership with Suez Lyonnaise des Eaux and ETPM, Entrepose can now consider expanding its operations throughout the oil-rich Caspian Sea region (comprising Kazakhstan, Turkmenistan, etc.). With a network of 60 permanent agencies in France, Delattre-Levivier can support expanding industrial firms, assisting them with their installation, renovation and transfers of equipment, maintenance, and operating assistance.

This company's 1998 revenues were roughly unchanged at 150 million euro (FRF 1 billion). Delattre-Levivier won three new multi-year service contracts in 1998, for Dexel-Sita in the Paris region, a logistics and transit contract for the CNES (French national space agency) in Guyane, and a contract for Esso at Port-Jérôme.

Delattre-Levivier won a

Groupe GTM acquires Hong Kong's second-largest car park operator

Les Parcs GTM has acquired Hong Hong's second-largest car park operator, Adams Parking, a service provider that operates more than 100 car parks in Hong Kong with a capacity of more than 30,000 spaces. Following this key international development, Les Parcs GTM now operates 200,000 parking spaces in 67 cities in France, and in 6 other countries.

The "Pont de Normandie," built by Groupe GTM.

contract from Sanofi to build a piping network at Aramon in the Var Department of France. Lastly, it added a new subsidiary, SECMI, based in La Rochelle, to its network of regional units.

Electrical contracting

GTMH reported revenues in the region of 580 million euro (FRF 3.8 billion) for 1998, an increase over the 1997 figure chiefly due to non-French sales, which now exceed 25 percent of the total, whereas French revenues remained stable.

The general export climate was favourable, even though falling oil prices weakened the financial situation of certain producer countries where GTMH operates.

In France, while some GTMH units reported flat revenues, others registered strong gains. There was sharp growth in sales of operating aids and traveler information systems for public transportation in Paris and other major cities in France and the rest of Europe, making GTMH a front-rank player in this sector.

GTMH also intensified efforts to position itself to grasp whatever opportunities arise to win global maintenance and outsourced services contracts in the main areas of manufacturing and the service sector.

Offshore engineering

ETPM specializes in offshore design, project engineering and infrastructure contracting for the oil industry. It registered strong sales growth in 1998. Revenues increased by 23 percent compared with 1997 to 723 million euro (FRF 4.7 billion), the Group share of this total amounting to 640 million euro (FRF 4.2 billion).

Completion of phase 1 of installation of the Elgin-Franklin pipeline in the North Sea for Elf Aquitaine accounted for a significant percentage of this increase. This project, one of the largest ever in the region, was completed on schedule, demonstrating ETPM's capacity as prime contractor to manage a large-scale operation, including all technical aspects.

Two significant events in 1998 were:

- the termination of ETPM's partnership with J. Ray MacDermott and the acquisition of MSCL, now ETPM DeepSea. This strategic move has opened up the market to ETPM for deep offshore or subsea operations.
- the winning of two contracts on Girassol, off the coast of Angola, for Elf. The contracts are worth in excess of 457 million euro (FRF 3 billion) to ETPM.

This initial major success is a practical outcome of ETPM's growth strategy. Further spending on R&D is enabling ETPM to develop the equipment needed to consolidate its position in conventional offshore work and to meet the challenges of new conditions in the oil market. This subsidiary will continue to establish itself as a major global player in the fast-growing subsea and deepwater sectors.

SGB's headquarters. SGB is one of Belgium's oldest companies.

Société Générale de Belgique

Etienne Davignon
Chairman, Société Générale de Belgique

“1998 was an exceptional year for la Générale in more ways than one, in terms of first-class earnings, and major operations that have left their mark on the Group in terms of its equity investments and shareownership.”

Christine Morin-Postel
Chief executive Officer, Chairman of the Management Committee, Société Générale de Belgique.

Société Générale de Belgique has been an almost wholly-owned subsidiary of Suez Lyonnaise des Eaux since Summer 1998. It in turn is the majority shareholder of Tractebel, the Group's energy arm, and the lead shareholder in several front-rank financial services and industrial companies. SGB's equity holdings comprise:

- Tractebel, a global industrial energy (electricity and gas) and municipal services group (see pages 24-26 and page 39),
- Fortis B, which has become one of Europe's foremost financial services, insurance and investment management groups since its merger with Generale Bank in 1998 (see page 52),
- Union Minière, a world leader in non-ferrous metals (see page 53),
- Arbed, a Luxembourg steelmaker that ranks among the world leaders
- Recticel, a European group specializing in the production of polyurethane foam.

The past year brought a rich crop of earnings and achievements.

Consolidated net current income for 1998 was up 8.4 percent, after 7 straight years of steady growth, making a record run in the company's 175 years' history. This performance bears out the wisdom of SGB's strategy over the past 10 years.

SGB provided substantial support, in 1998, in the creation of a new European financial group. The disposal of SGB's 29 percent shareholding in Generale Bank set the scene for Fortis to build a new integrated banking group around G-Banque, capable of rivaling its main competitors. In keeping with its commitments, SGB has reduced its holding in Fortis B, reverting to the premerger level (20 percent). The Group will benefit from expected annual synergies of the order of 675 million euro from 2002 onward.

In the middle of 1998, Suez Lyonnaise des Eaux launched a share exchange offer for the remaining SGB shares outstanding. This successful bid, worth nearly 4 billion euro, helped to strengthen the Group's Franco-Belgian identity and confirmed energy's position among Suez Lyonnaise des Eaux's core businesses.

In 1999, SGB acquired Elyo from Suez Lyonnaise des Eaux, in order to build a single energy division centred on Tractebel, with responsibility for the conduct of all Suez Lyonnaise des Eaux energy sector businesses. An energy Committee, consisting of the top managers of Suez

On the occasion of the 175th anniversary of SGB, their royal highnesses the King and Queen of the Belgians met the managers of SGB. Seen here, the official ceremony to inaugurate the Magritte exhibition in Brussels, sponsored by SGB.

Lyonnaise des Eaux, Société Générale de Belgique and Tractebel, will meet regularly in order to maintain a constructive dialogue between management and the shareholders. This committee will contribute to the coordination of the energy division with Suez Lyonnaise des Eaux's global strategy. SGB's net current income rose thanks to strong performances by Tractebel and the new Fortis-Generale Bank entity. Its contribution to Suez Lyonnaise des Eaux's net current income amounted to 0.31 billion euro, or 40.4 percent of the total. SGB's exceptionally high earnings (representing a 17.3 percent net return on equity) reflect the wisdom of the strategy of many years' standing, based on recentering on the most profitable businesses and pushing ahead with international development. Tractebel and Fortis accordingly received strong support from the SGB in their efforts to expand in Europe and the rest of the world.

Fortis (B) is now Europe's tenth-largest financial group, while Tractebel is the no. 1 private independent electricity group in Europe, and the world's no. 3 independent electricity producer.

Tractebel and its subsidiaries Electrabel and Distrigaz enjoy strategic positions in electricity and gas, trading and project engineering. They can therefore look with confidence to the new challenges being created by deregulation in Europe, and by the worldwide trend to privatization of municipal services.

Fortis, fortified and renewed

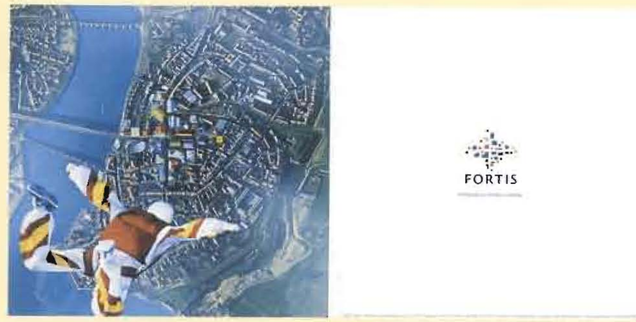
Fortis emerged from the events of 1998 renewed and fortified. Renewed by the reorganization of its management and streamlined operating functions; fortified by the merger with Generale Bank. Several measures will boost transparency and efficiency. These notably concern the names of listed companies(1), shares, and the management of Fortis. The names of the listed companies have been modified: from Fortis AMEV to Fortis (NL), and from Fortis AG to Fortis (B). Respectively 2-for-1 and 9-for-1 stock splits have placed the shares on an equal footing, and they now carry equal earnings entitlements. Following the merger with Generale Bank, Fortis now forms a strategically coherent group. It has also considerably strengthened its market positions. In the Benelux especially, Fortis now leads the market in asset management, services to SMEs and in private banking, and is in third place in corporate banking.

Fortis also leads the market in bancassurance.

The Group has also powerfully consolidated its positions outside the Benelux.

(1) Fortis has two identical shares: Fortis B, listed in Brussels, London and Luxembourg, and Fortis NL, listed in Amsterdam, London and Luxembourg. Fortis NL is traded under a sponsored ADR program in the United States.

Sometimes one merely has to take a fresh look at things for new ideas to emerge. That was the thought that inspired Fortis' new logo, symbolizing the diversity of its customers and their needs.



FORTIS B

MAURICE LIPPENS
CHAIRMAN AND
CHIEF EXECUTIVE FORTIS B

Fortis is an international insurance, banking and investment management group. It helped to pioneer bancassurance, and it is one of the leading integrated financial services providers on its domestic market, the Benelux. The group provides a full line of financial services to individuals, businesses and the public sector in the Benelux. Fortis focuses on specific market segments in the rest of Europe, the United States and Asia.

"Fortis had an excellent year in 1998, achieving 17 percent organic growth. It was practically untouched by the crises in Asia, South America and Eastern Europe. The wave of concentrations in the financial sector, market volatility and the downtrend in interest rates helped to generate substantial capital gains and high earnings on financial transactions."

Net income for the Group came to 1,786 million euro in 1998, with total assets of 338 billion euro at the end of 1998. The Group intends to achieve a minimum return on equity of 12 percent and an annual growth in earnings per share of between 7 and 12 percent. Fortis' market capitalization stood at 24.6 billion euro at the end of 1998.

Fortis seeks to operate on those markets or market segments where it can hope to play a preponderant role while continuing to grow. Its key strength lies in its business mix, with their solid roots in their markets and strong customer relationships, and in the combination of its different companies. These allow Fortis to offer a broad product range, backed by considerable financial strength, while spreading its risks and building up a wealth of knowledge. Regional flexibility is thus combined with global power.

A new operating structure for Fortis

Fortis extensively reorganized its operating structures in the second half of the year, discarding its geography-based organization in favour of one based on marketing channels.

The insurance Group is made up of companies that mainly market its products through third parties such as independent brokers, agents, or the bank branches of outside companies. Fortis' banking activities have been integrated in order to consolidate its position as a leading financial services provider in the Benelux. Another purpose of this more is to create a solid platform from which to expand in Europe and other markets, and to achieve significant synergies yielding additional savings and revenues. Fortis bolstered its positions in the United States in 1998, successively acquiring Pierce National Life Insurance, John Alden Financial Corporation, and then Bankers Insurance, another American company.

The outstanding event of 1998 was the acquisition of Generale Bank and the Belgian State's remaining 25.1 percent interest in CGER.

A growth strategy for Fortis

Growth, whether organic or the outcome of selective acquisitions, has always been a key feature of the Group's strategy. But it has never been an end in itself; its prime aim is to help improve profitability. From its enhanced position on its domestic market, the Benelux, the Group has built up a solid springboard for further growth in Europe, the United States, and Asia.

Suez Lyonnaise des Eaux financial activities

- **Union Minière (via SGB)**
  Union Minière's interests span the extraction, smelting, refining, processing and recycling of non-ferrous metals
- **Sofinco**
  This bank specializes in consumer lending; it is no. 2 in consumer credit in France.
- **Suez Industrie**
  Venture capital
- **Coficem/Sagem**
  Sagem is France's no. 2 telecoms equipment group; it is also a leader in automotive and defense electronics.

Other affiliates

Union Minière

Union Minière is a world leader in nonferrous metals It produces and commercializes more than 20 precious and special metals for use in high-tech applications in particular.

In 1998, the group was hurt by especially adverse economic conditions characterized by historically low prices, an unstable dollar, deteriorating processing and refining conditions, and weak sale prices. To these were added the effects of the crisis in Asia and sharper competition. Moreover delays in the start-up of the new smelter at Hoboken (Belgium) severely impacted the firm's operating income. Union Minière immediately took appropriate steps to cover its operating risks by means of additional provisions and reorganizing its core businesses. The group expects to recover its room for maneouvre progressively, allowing it to achieve the targets originally stipulated in its industrial development plan.

Sofinco

In April 1998 Suez Lyonnaise des Eaux announced the sale over two years of 100% of the capital of Sofinco for 1.39 billion euro (FRF 9.15 billion).

Le Crédit Agricole Indosuez thus holds 70 percent of Sofinco in 1999, and is expected to acquire the remaining 30 percent in 2000.

Suez Industrie

Suez Industrie, a venture capital subsidiary, registered very strong earnings in 1998. It did so while continuing to reorganize in keeping with its strategy of reducing group equity invested in this sector.

Main disposals during the year were Eco Arc in France, the partial disposal of ACS in Spain, and Howmet Turbines in the USA. Disposals of longstanding investments totaled 188 million euro (FRF 1.2 billion), yielding 105 million euro (FRF 690 million) in capital gains.

This company is in the process of strategically redeploying away from proprietary investing activities and toward the management of third-party funds. This policy materialized most spectacularly in 1998 in the launch of the 180 million euro (FRF 1.2 billion) Fonds Astorg II, to which Suez Industrie itself contributed only 45.7 million euro (FRF 300 million). Suez Industrie also formed its own independent fund management company, Suez Capital Partenaires, which was approved by the Commission des Opérations de Bourse.

The other funds backed by Suez Industrie, namely Mercapital in Spain, Suez Asia Equity Associates in Asia, together with Suez Technology Fund and Suez Equity Investors in the United States, invested a total of approximately 76.2 million euro (FRF 500 million).

Suez Industrie intends to pursue the same approach in 1999, sponsoring further venture capital funds in Germany, to be managed by Suez Finanzberatung. In 1998, Suez Industrie contributed 85.25 million euro (FRF 522 million) to Suez Lyonnaise des Eaux's 1998 consolidated income, and paid it a dividend of 122.48 million euro (FRF 750 million).

Coficem/Sagem

Sagem is an international high-tech group with consolidated sales of 2,9 billion euro (FRF 18,70 billion) in 1998. Sales outside France accounted for 42 percent of this figure. Sagem is France's number two supplier of telecommunications equipment as well as a leader in automotive and defense electronics. It operates in more than 20 countries, with production facilities in Germany, Brazil, Spain, the United States, and the Czech Republic.

In March 1999, Suez Lyonnaise des Eaux took the 20% participation of SGB in Coficem / Sagem.

The XIIIth Innovation Awards ceremony, Paris

INNOVATION AND RESEARCH

Innovation is a priority at Suez Lyonnaise des Eaux, for only by innovating can we meet the challenges of internationalization, deregulation, and the environment. The keys to innovation are the motivation and creativity of all workers, and proactive research and development.

Everyone at Suez Lyonnaise des Eaux is encouraged to play a part in developing new innovations, and the best innovations are distinguished at an annual awards ceremony: 35 in 1998 in services. A fund is available, moreover, to help innovators develop and complete their projects.

Innovation can apply to every area of the Group's activities, including marketing, finance, technology, human resources, and may take place in any country. To illustrate the point, two grants made in 1998 were for a youth employment project and a project outside France for young technicians. The Group gave its backing to Lyonnaise des Eaux for a large-scale World Bank-sponsored study of alternative methods for supplying water to poor neighborhoods in the emerging countries.

Suez Lyonnaise des Eaux ranked top in 1998 in the annual survey of innovation in business carried out by the French magazines La Recherche and La Tribune.

A proactive, increasingly international, R&D effort is the bedrock of this drive for innovation. Key themes covered include the environment, more effective responses to customer needs around the world, and developing advanced systems and methods to improve quality and cut costs.

Energy

In 1998, Elyo launched an experimental decentralized waste-to-energy air-conditioning system in Besançon (France). This utilizes the heat generated by waste incineration in summer. In Casablanca, Elyo has developed combined water-electricity systems in order to cut distribution costs.

Tractebel continued to improve the quality of electricity supplied to industrial plants, modulating the current to meet their precise needs. It continued work on the processing and final storage of radioactive waste in keeping with Belgian Government guidelines. In partnership with several teams of scientists, Tractebel has developed software capable of calculating a suite of values for each energy system, covering primary energy consumption, environmental emissions and external costs, including the costs and energy needed to build the equipment used, maintenance, after-life demolition, and replenishment of energy reserves. This method also furnishes a comprehensive ecological and economic assessment, enabling operators to select the energy system best-suited to each context.

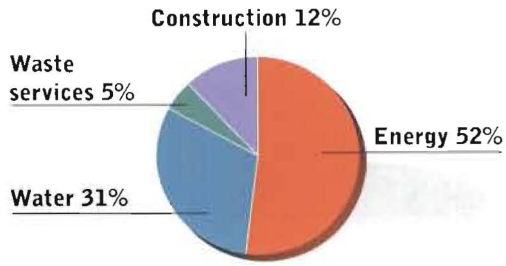
Water

Lyonnaise des Eaux has gained a significant strategic advantage in taking over water distribution systems. A new methodology devised at its Newcastle (UK) research center can quickly

Suez Lyonnaise des Eaux's research and development effort, 1998

Spending: 180 million euro (FRF 1.2 billion)
1,000 research projects
800 research workers
80 scientific publications
28 new patents filed
100 cooperative ventures with publicly-funded research

Breakdown of R&D spending by business sector



diagnose the condition and performance of an existing distribution system. This was successfully applied in the Atlanta bid, and is now used in numerous water services around the world.

The "RADAR" hydrological modeling software package, designed to optimize the treatment of rainwater, has been implemented at three sites (Paris-Orly, Genoa, and Malmö) for purposes of testing in various weather conditions. In a partnership with Thomson-CSF and Seres (an instrumentation maker), and with backing from the French Industry Ministry, Lyonnaise des Eaux and Degrémont have embarked on a 5.64 million euro (FRF 37 million) 3 years program to develop automated sewerage plant operating systems.

Finally, Lyonnaise des Eaux's worldwide research network mobilized swiftly on several occasions in 1998 tackled incidents of accidental contamination (including Sydney, Manila, etc.) successfully.

Waste services

Following the acquisition of BFI's non-American subsidiaries, Sita is now a major European operator and is reinforcing its R&D capability in consequence. It has set up a research center at Vernon, near Paris, and established a network of competencies for each line of business, run by the team in the most-advanced European country in the specialty concerned.

An onboard computer system developed by Sita is now fitted to its waste collection vehicles. This serves to optimize vehicle rounds and weigh containers for each category of waste, paving the way for wider use of selective waste collection.

The Vitrogel process, now on the market, stabilizes asbestos during removal of asbestos-based insulation, flocculation and transportation systems.

Communications

Lyonnaise des Eaux has enhanced its expertise in broadband communications combining digital TV, Internet access and telephony, now being deployed in interactive services to enable interactive TV program guides, electronic commerce, etc.

Construction

Groupe GTM is developing its management expertise in major transportation infrastructures (including tollroads, large bridges, car parks, airports, etc.). It is also enhancing its competencies in special industrial works (mechanical engineering, electricity, offshore projects, etc.). The use of linear winches to insert metal sheaths inside a chimney more than 200 meters tall inside the thermal electricity power station at Le Havre (France) was a world first. This technical exploit illustrated the Group's technical expertise in lifting very heavy loads and in rapid, special welding. DUMEZ-GTM and GTM Construction recently completed the replacement of suspension cables on the Pont de Tancarville bridge (France), carrying out this very delicate operation with no interruption of traffic, in line with the sophisticated calculations in which the Group accurately predicted the load shifts measured during transfer operations.

The exact positioning of the foundations of piles for the Rion-Antirion bridge, in Greece, was validated by simulations and testing on scale-models in a centrifuge. This research was presented in a widely-noted communication to the European Paraseismic Engineering Conference.

Finally, in a partnership with Lyon's Claude Bernard University, GTM Construction has developed a carbon fiber textile process for repairing cracked civil engineering structures.

Signature of the international charter of labor relations, in Poitiers. This charter is a formal statement of the values that underpin the Group's human resources policy and its commitment to youth employment.

HUMAN RESOURCES

With more than 201,000 employees worldwide, Suez Lyonnaise des Eaux is now one of Europe's largest employers. Harnessing cultural diversity and uniting talented men and women around powerful values, in support of a clear industrial and international strategy: these are key tasks facing the Group's human resources division.

Close-knit, multicultural, professional teams, welded for success

Determined efforts to recruit internationally, combined with proactive measures to promote internal mobility, are helping to build multicultural teams. They are also forging a common Group culture and sense of professionalism worldwide, thus giving the Group a genuine competitive edge. Annual evaluation interviews, careers management committees and "Job News," the in-house jobs exchange now posted on the Group's Intranet, are the main vehicles through which this policy is being pursued.

Each business segment consults regularly with the Executive Board in monitoring and planning the careers of some 1,500 present and future senior managers in France, Belgium and the rest of the world. In fact, though, a high premium is placed on identifying and nurturing talent at all levels of the Group, so as to serve customers and partners more effectively.

Welding teams into a cohesive force also implies giving them a larger stake in the challenges facing the Group and in its results. In 1999 a major priority is to expand the Group's employee shareownership.

State-of-the-art training facilities are part of the continuing drive to create value

The Suez Lyonnaise des Eaux Institute worked with the Committee of Future Issues, Innovation and Management in 1998 to provide career support and stimulation to top managers.

The Institute organized some 7,000 hours of seminars and forums at its Fillerval Center, on topics ranging from general management to strategy, leadership, and behaviour. The Institute is establishing itself as the Group's cultural melting pot.

However, the Group has grown so large, and the international issues are so complex, that a fully-fledged Suez Lyonnaise des Eaux University is scheduled for launch as soon as 1999. With its greatly expanded human, teaching and physical resources, this campus based in Europe will also have extensions in the United States, Latin America and Southeast Asia. It will train young high fliers destined for top management posts, with a strong emphasis on promotingmulticulturalism, shared values and knowledge, identifying talent and helping it to blossom.

Suez Lyonnaise is working with leading experts and in close association with the academic world to broaden its managers' cultural horizons.

The Suez Lyonnaise des Eaux team partnered EM Lyon at this year's international Euromanager tournament,

Unexercised stock options (share subscription and purchase options)

	Ex-Suez plan 1994	Ex-Suez plan 1996 (1)	Ex-Lyonnaise des Eaux plan 1994	Ex-Lyonnaise des Eaux plan 1995	Ex-Lyonnaise des Eaux plan 1996	Suez Lyonnaise des Eaux plan 1997	Suez Lyonnaise des Eaux plan 1998 (1)
No. of option holders	49	59	273	354	421	868	971
Corresponding no. of shares	74,608	82,107	268,250	321,950	401,650	994,200	1,040,700
Percentage of capital	0.05	0.06	0.18	0.22	0.27	0.67	0.70

At December 31, 1998, the number of shares to be issued represented 2.15 percent of the capital (undiluted).
(1) Purchase options.

and represented France at the finals in Macao to finish 6 [th].

An International Charter of Labor Relations to affirm our social and human values.

The Suez Lyonnaise des Eaux International Charter of Labor Relations was signed in Barcelona on October 9, 1998 by Gérard Mestrallet and Philippe Brongniart, and by the European consultative committee. The charter sets out the values that preside over the Group's human resources policy and the fundamental rights of personnel the world over.

This charter is the culmination of a joint effort over several months by the international human resources review committee, the European consultative committee, and the Suez Lyonnaise des Eaux Group human resources division. This International Charter constitutes a solid basis for labour-management dialogue and is an expression of a shared desire for transparency. It is the first document of its kind to be signed within an international corporation. It now forms an integral part of the Suez Lyonnaise des Eaux Ethical Charter.

A relentless commitment to jobs

The debate on the 35-hour working week in France served as an opportunity to reflect on the present work organization, and even to reform it in some cases. Several Group companies entered into decentralized negociations on the reorganization and reduction of working hours.

The group's commitment to youth employment is nothing new, having found jobs or trainee positions for 9,000 young people since 1994. But it is pursuing these efforts with untiring determination, in conjunction with a number of loyal and active partners:

- 14 regional conventions were signed with local authorities, including Dunkirk, Hagueneau, Nancy and Bordeaux in 1998, to help find work for young job seekers, reflecting the continuity of the Group's action in this sphere;
- in Belgium, Electrabel has pledged to take on 3,000 job seekers, many its Tihange plant;
- further expatriate job contracts have been signed for 200 young international technicians, to whom the Group is offering international job experience and a chance to learn about different cultures;
- youth employment programmes, particularly in the waste services and water business segments, are demonstrating the personal involvement of Group employees;
- a vigorous multi-year mentoring training programme. Long an integral part of the Group's culture, mentoring is designed to help transferor knowledge to the younger generations;
- each Group company strives to ensure that 2 percent of its workforce at all times consists of young people enrolled in alternating work-study schemes leading to qualifications.

By promoting and stimulating decentralized programmes with long-term partners, the Group is not only discharging its duties as a corporate citizen with regard to the young, but is also combining sound management with innovation.

Spring gives employees a stronger stake in Group growth

More than 20,000 employees subscribed 31.7 million euro (FRF 207 million) in 1998. Altogether, more than 38 percent of those eligible are already shareholders. Suez Lyonnaise des Eaux wants to give Group employees a stake in its successful performance, increasing their shareholding from 1 to 5 percent of the capital in the comming years. Operation Spring, in 1999, sought to involve all Suez Lyonnaise des Eaux personnel in France, Belgium and the rest of the world. What made this operation original was it international character, enabling everyone all over the world to display their confidence in the Group's development strategy.

Group head count

	31/12/97	31/12/98
Total work force	175,000	201,000
Total work of which non-French employees	100,000	126 ,500

GROUP VALUES

A year ago, Gérard Mestrallet declared that establishing clear values for the Group was a priority. "We must complete the task of building shared values," he said. The idea is to "successfully create unity within the Group, to build a sense of identity, to put synergies to work," and to assert our vision of the future through unambiguous behavior. To achieve that, we needed to find the highest common denominator transcending the multitude of business sectors, skills, cultures, locations, and so forth.

A wide-ranging survey was sent out to the Group's 201,000 employees.

Independent consultants in France and abroad held round tables on the subject.

Six values emerged from these consultations as central to the philosophy of the Group. They are the basic building blocks of professional conduct for all Suez Lyonnaise des Eaux personnel.

As Jérôme Monod puts it, this approach "had the great merit of establishing a set of universal principles for the Group in keeping with its global ambitions."

Our six values

Professionalism, partnership, teamwork, value creation, environment, and ethics.

• **Fostering professionalism,** the key to better customer service the world over.

• **Partnership:** partnerships built on trust and the long-term view help build transparent, balanced relationships with our opposite numbers.

• **Teamwork,** to promote the spirit of enterprise, innovation and creativity, strengthening bonds of solidarity, and synergy.

• **Value creation,** to increase profitability and financial strength, the keys to the corporation's independence and continuing existence.

• **Environment:** respecting the environment for lasting improvements in the quality of life.

• **Ethics:** ethical standards applicable to all, to make these values a living reality in a climate of mutual respect.

Ethics

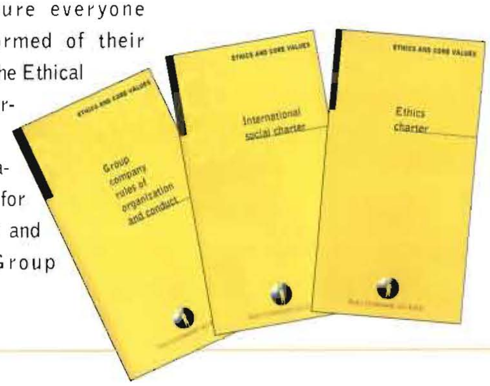
Ethical conduct will always be a matter of individual responsibility, in the last analysis.

But each company must nevertheless establish procedures to foster the emergence of a shared ethic. Like the Supervisory Board of Suez Lyonnaise des Eaux, the Boards of the main companies have set up Ethics committees to oversee the individual and collective values that are the bedrock of the Group's activities. Each company chairman, moreover, has appointed an "Ethical compliance officer." This is a staff position, with responsibility for dealing with ethical issues, proposing, formulating and circulating codes of conduct, enforcing compliance with codes and charters, and reporting on the application of ethical rules. Group compliance officers meet regularly to share their experiences, and all employees can contact them for advice on how best to comply with the Group's ethical rules.

"Ignorance of values is no excuse"

Suez Lyonnaise des Eaux's clearly-formulated and identified values are the engine at the heart of the Group. But it is up to each individual to make those values a living reality, and to pass them on to their entourage inside the Group and in their business dealings. The Group has published a number of documents to ensure everyone is properly informed of their obligations, i.e. the Ethical Charter, the International Charter of Labor Relations, and Rules for the Organization and Conduct of Group Companies.

These documents, available in French, English, German and Spanish, were formally approved by the Executive Boards before being submitted to the Ethics Committee and to the Supervisory Board, which gave them its wholehearted approval.



ENVIRONMENT

Protecting the environment is a central issue in each of the Group's businesses. Treating waste water or handling waste are both directly designed to reduce the impact of human activity on the environment. Energy management, water distribution, and the construction of infrastructures, meanwhile, transform natural resources into the goods and services that are indispensable to human life.

Each Suez Lyonnaise des Eaux business is responsible for defining its priorities and applying environmental policies geared to its strategy, regulatory conditions and customers' demands. The main aims of these policies are:

- to analyze continuously the environmental impact of activities, in order to make long-term improvements to the quality and safety of facilities, and to manage attendant risks,
- to minimize pollution caused by companies' activities,
- to economize natural resources and preserve ecosystems.

In the energy sector, Tractebel and Elyo have for years been developing cogeneration and trigeneration technologies, which cut energy consumption and greenhouse gas emissions. Electrabel has designed a methods for analyzing the CO2 emitted by its production units, in order to propose to the Belgian Government measures for meeting international targets.

A substantial proportion of research spending in the water sector is aimed at protecting natural resources, by recycling waste water, replenishing groundwater, or investigating the consequences of natural phenomena such as global warming.

In La Paz (Bolivia), Aguas del Illimani (a subsidiary of Suez Lyonnaise des Eaux) analyzes changes in glaciers in order to predict the evolution of resources and forecast investment needs more accurately.

Another major issue on which several Group business sectors are working is the recycling of sludge produced from the treatment of effluent (see box). The main focus of investigations in waste services is on analyzing and modeling the long-term behavior of landfills, in order to prevent public health risks, and on sorting and recycling waste in order to cut consumption of natural resources.

In the construction sector, Groupe GTM is concentrating on ways to integrate its structures into the environment, reducing environmental damage associated with its projects, the reuse of materials after demolition, and the use of clinker in constructions processes.

Auguas Argentinas helped to restore the Coipos nature reserve, Buenos Aires. This project preserved plant and animal species, and restored the aquatic ecosystem.

NORTHUMBRIAN LEADS THE AWAY IN ENVIRONMENTAL PROTECTION AND TECHNOLOGY

In response to new UK and European Union directives, Northumbrian Water (a 71 percent-held subsidiary) recently inaugurated the £ 70 million state-of-the-art Bran Sands Sludge Treatment Center. This now treats sludge for municipal and industrial clients. This plant converts the sludge produced from the treatment of effluent into biopellets, thereby respecting Northumbrian's obligation to end the disposal of sludge in the North Sea, and saving 350,000 tons of coal per year.

Biopellets

The sludge is dried, then compressed, to produce tiny pellets (of between 4 and 12 mm diameter). These pellets are cooled before being conveyed to dry silos via a pneumatic system, for subsequent use as fuel, agricultural fertilizer, and even in the manufacture of building bricks.

Investors' club

Suez Lyonnaise des Eaux is constantly seeking to improve its performance, in the interests of shareholders, investors and employees alike, so that all can share the benefits of the value thus created. A year-round schedule of regular contacts with individual and institutional investors enables the Group to keep closely in touch with their needs and concerns.

Suez Lyonnaise des Eaux
espace actionnaires

SHAREHOLDERS' CLUB

More than 300,000 shareholders have chosen to stay with the Group as it develops. In order to deserve that confidence, Suez Lyonnaise des Eaux has made a series of firm pledges concerning earnings growth and return on capital employed, as well equality of treatment for all shareholders, and financial disclosure.

Working closely with the Shareholders' Advisory Committee, Suez Lyonnaise des Eaux has enriched the various channels that keep shareholders regularly informed of events concerning the Group.

The Committee held 3 working meetings in 1998, but it was also consulted regularly by telephone, and it attended several site visits and briefings held in the provinces.

The Group Advisory Committee is a forerunner to the European Committees. It consists of 10 French and 5 Belgian members, selected for their profile, career, motivation, with care taken to ensure a satisfactory geographic and linguistic spread (in the case of Belgium). The Committee advises the Group on ways to improve communications with individual shareholders, and makes various recommendations.

SHAREHOLDERS' CLUB

This Club serves as a focal point for exchanges of views and information. It seeks to develop a better understanding of the Group and topics of interest to shareholders such as the stock market, the euro, and the Internet.

More than 26,200 shareholders have joined the Shareholders' Club since its foundation in February 1998. Membership was broadened to include Belgium in December 1998, in the wake of an advertising campaign in the press : 1,200 members then joined.

CLUB BENEFITS

Regular information sent direct to your mailbox

- **Shareholders' newsletters:** 3 or 4 times a year, with news of the Group's businesses, share data, and Club news, etc.
- **Annual and interim reports:** all the well-informed investor needs to know to understand the Group's earnings, strategy, and outook.
- **Shareholder's handbook:** rights, taxation, how to read stock market listings, where to find out more about the share, the euro, the Shareholders' Meeting, and a glossary of terms.
- **Report on the Annual General Meeting of Shareholders:** for those unable to attend the AGM, a report on the meeting (highlights, questions from the floor and freephone number) will be sent out on application (call Shareholders' freephone number in France and Belgium).

Visits and meetings several times a month

- Visits to sites in France and Belgium, including cogeneration plants (Energy), drinking water plants (Water), a sorting center (Waste services), and M6 studios (Communications), among others.

Suez Lyonnaise des Eaux shareholders can see the Group's businesses firsthand several times a year.

- Shareholders' briefings: Suez Lyonnaise des Eaux organizes several briefings a year for individual shareholders, attended by senior Group officers. These meetings are organized in conjunction with the Société des Bourses Françaises, and with investment magazines in France and Belgium.
- Stalls at the leading investor fairs (with free invitations for Club members).

Specialized training programs

• The Paris Stock Market School (L'Ecole de la Bourse): these one-day sessions are organized in conjunction with SBF-Bourse de Paris and 2 Belgian investment magazines. Their aim is to promote investors' understanding of stock market mechanisms.

• How to use the Internet: this program, organized in association with our subsidiary Lyonnaise Câble, provides an introduction to the possibilities of cable-based Internet access, explaining how to surf the Group website dedicated to its shareholders, and how to browse the Worldwide Web at will.

• Euro-all you need to know. The euro is now a fact of life. We want to help familiarize our shareholders with the ins and outs of the euro between now and 2002.

OUR PRIORITY, DEVELOPING AND IMPROVING DIALOGUE WITH OUR SHAREHOLDERS IN REAL TIME

We have introduced an array of systems for that purpose:

• Freephone numbers, respectively: 0800 177 177 in France and 0800 25 125 in Brussels. These numbers, operated directly by the Financial Communications Division's Shareholder Relations Department, are open year-round, from Monday to Friday, betwen 9:00 am and 1:00 pm, and 2:00 pm and 6:00 pm. We are committed to answering legal, financial and Group-related queries rapidly and in detail.

• A dedicated shareholders' Internet site: www.actionnaires.suez-lyonnaise.com. This site contains several areas devoted to share information (real-time stock quotes, euro-franc converter), the Club pages (the ins and outs of the euro, reports on site visits), library (download speeches by the Chairman and President, annual and interim reports, shareholders' newsletters), chat room (ask questions and leave e-mail messages for members of the Shareholders' Advisory Committee).

ANALYSTS' AND INVESTORS' WEBSITE

Suez Lyonnaise des Eaux kept up a steady flow of information for analysts and investors in 1998.

For analysts:

• more than 50 one-on-one contacts in Paris,

• more than 500 telephone interviews,

• more than 400 analysts met on the occasion of road shows (earnings, major operations, etc.) and the Shareholders' Meeting.

For investors:

• more than 100 one-on-one contacts in Paris,

• more than 700 investors met on the occasion of seminars, conferences, and site visits,

• 20 road shows outside France, in the leading international financial centers.

Via our English-language website:

www.finance.suez-lyonnaise.com is dedicated to institutional investors and analysts (20,000 pages visited monthly, more than 1,000 subscribers), featuring an exclusive Chairman's editorial, on-line press releases in real time, answers to frequently-asked questions, financial presentations, and the annual report. All this information is downloadable and available for 24-hour consultation from all around the world.

CONTACTS

Financial Communications: Valérie BERNIS

• Individual shareholder relations:
Valérie WARD, Rita RIO-freephone (France) 0800 177 177

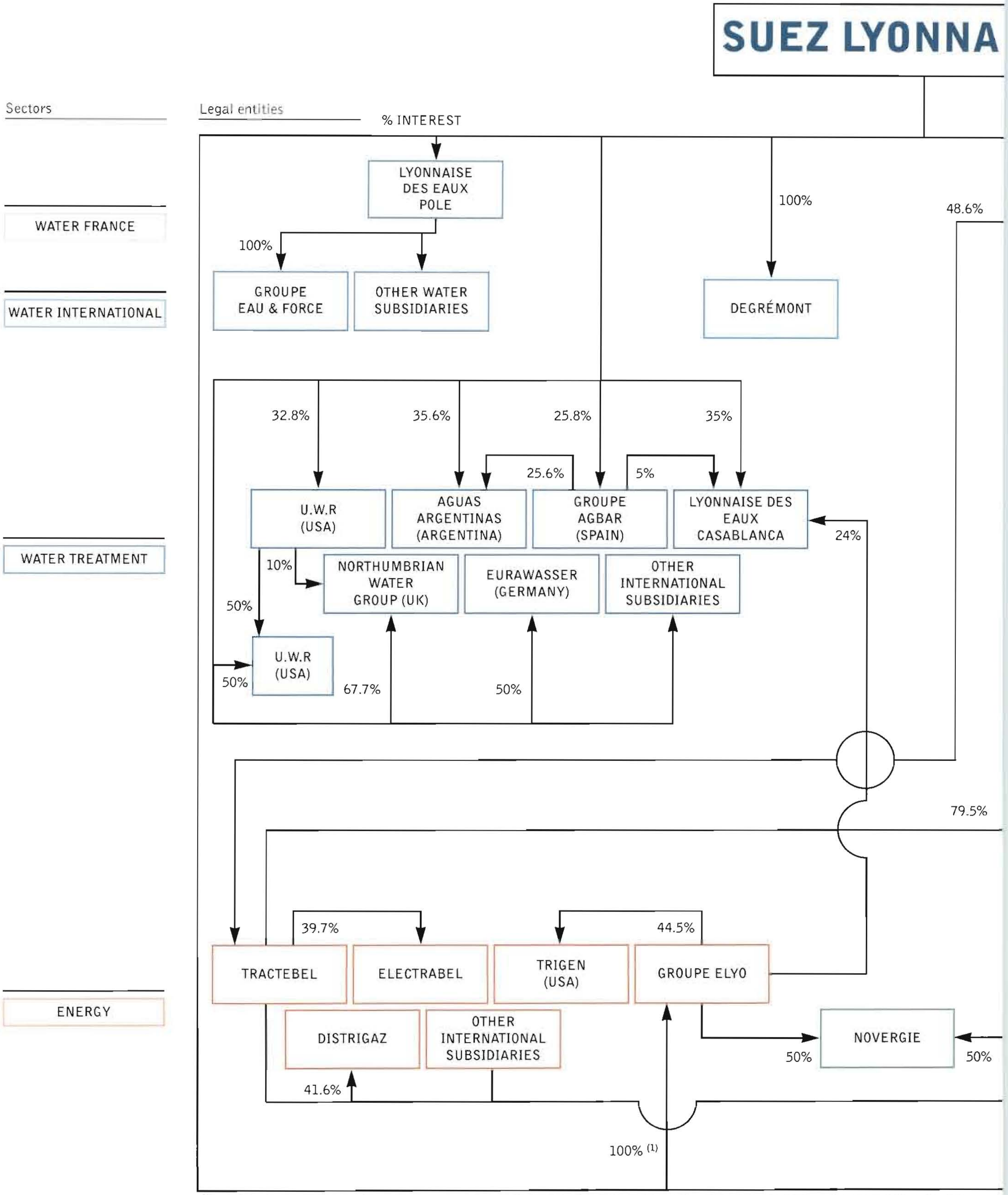
• Relations with analysts and investors:
Patrick AYOUB, Isabelle JOUET PASTRE

• Financial communications in Belgium:
Guy DELLICOUR- freephone (Belgium) 0800 25 125

Upcoming Suez Lyonnaise des Eaux events:

• Annual General Meeting of Shareholders	May 28, 1999
• Dividend payment:	June 1, 1999
• Half-yearly results:	October 7, 1999
• Annual results:	March 2000

SIMPLIFIED ORGANIZATION CHART



(1) On March 31, 1999, the Supervisory Board of Suez Lyonnaise des Eaux approved the sale of Elyo (100 percent) to Société Générale de Belgique and the purchase by Suez Lyonnaise des Eaux of Société Générale de Belgique's 20 percent equity holding in Cofigem/Sagem

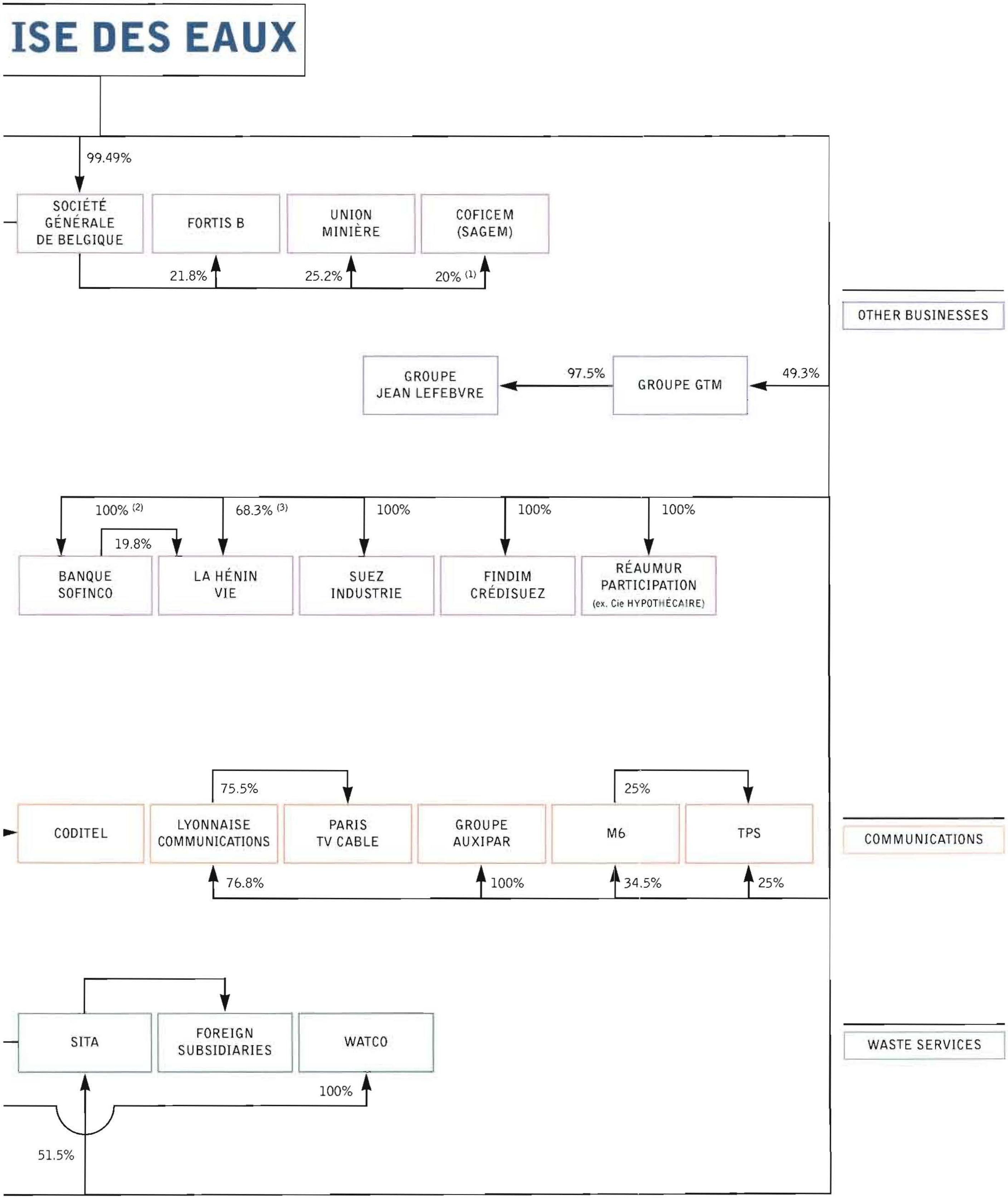
(2) According to the terms of the Sofinco disposal in April 1998, the shareholding is 30 percent in 1999, falling to 0 percent in 2000.

(3) Disposal of La Hénin Vie, January 1999.

(4) 48.6% of interest 50.1% of control.

(5) 50.4% of control.

AT DECEMBER 31, 1998



Claude Monet at work.

Management report

GENERAL COMMENTS

The main features of Suez Lyonnaise des Eaux's consolidated financial statements for the 1998 fiscal year were as follows:

- Growth: revenues generated in the core businesses amounted to EUR 21.42 billion, up 17% on 1997, with the share generated on the international market increasing to 37% (27% in 1997).
- Profitability: a Group share of net income amounting to EUR 1.01 billion (+64%), of which EUR 0.76 billion was the Group share of net current income (+25%) and EUR 0.24 billion was the Group share of net extraordinary income.
- Conservatism principle: contingency and loss provisions in the balance sheet increased by 19%, amounting to EUR 8.28 billion.
- Financial flexibility: major development operations and operations to refocus on the core businesses did not undermine the Group's solid financial position. This is illustrated by the debt equity ratio of 59% and the ratio of coverage of interest expense by gross operating results (EBITDA, excluding the financial sector) of over 7.5.

Consolidated **revenues** amounted to EUR 31.36 billion, up 8% compared to 1997.

Revenues generated in the core businesses made up 68% of the total. There was pronounced growth in the core businesses of Energy, Waste Services and Communications (up by 10%, 48% and 10% respectively).

Others contributed EUR 9.94 billion, of which almost two-thirds were generated in the construction sector.

Operating income amounted to EUR 2.8 billion, making up 8.9% of revenues compared to 7.9% in 1997. The improvement in operating profitability is a result of the strengthening of the Group's interests in companies with high operating profitability.

There was a **financial loss** amounting to EUR -0.37 billion compared to EUR -0.3 billion in 1997. This was primarily due to the impact of the reclassification of leasing contracts as from January 1, 1998 (EUR -0.05 billion) and to the increase in average outstanding debt, which were partly offset by a slight reduction in the average cost of debt.

In total, **current income** of fully consolidated companies amounted to EUR 2.43 billion, up by 22%. This made up 7.8% of revenues for the year compared to 6.9% in 1997.

Extraordinary income amounted to EUR 179.6 million compared to an extraordinary loss of EUR -50 million in 1997. It is broken down hereafter, showing the net share attributable to the Group.

Corporate income tax, essentially consisting of due and payable taxes, amounted to EUR 0.64 billion. The financial statements for 1998 include a tax surcharge in France, with an estimated impact of EUR 13.7 million

The share of **income from companies accounted for under the equity method** amounted to EUR 0.26 billion compared to almost EUR 0.3 billion in 1997. This drop is due to the adoption of the full consolidation method by the Brazilian subsidiaries of Sita and to the Group's acquisition of an increased interest in the TPS digital TV channel package, which is currently in the start-up phase. These changes were partly offset by the performance of the financial subsidiaries of Société Générale de Belgique.

Total net income amounted to EUR 2.06 billion. **Minority interests** accounted for EUR 1.05 billion of this amount, essentially located in Tractebel and Electrabel, which are subsidiaries of Société Générale de Belgique.

The net Group share of income amounted to EUR 1.01 billion, up 64.3% compared to 1997 and broken down as follows:

Millions of EUR

	1998 FISCAL YEAR	1997 FISCAL YEAR
Net current income, Group share	762.7	609.0
Net extraordinary income, Group share	242.3	2.8
NET INCOME, GROUP SHARE	**1,005.0**	**611.8**

Thus, the growth in the Group share of net income stems from the 25% increase in net current income, accentuated by the increased contribution of extraordinary income.

Net earnings per share, calculated in relation to the average number of outstanding shares, after deducting treasury stock, was EUR 7.41 (compared to EUR 4.92 in 1997).

The total balance sheet amounted to EUR 72.49 billion.

Fixed assets were worth EUR 45.95 billion. **Goodwill** amounted to EUR 2.96 billion (i.e. EUR 2.02 billion, Group share), up by EUR 1.39 billion as a result of significant acquisitions in the Waste Services sector (including the acquisition of BFI's entities outside North America for EUR 0.85 billion and the purchase of the minority interests in Watco for EUR 0.17 billion), the Communications sector

(EUR 0.12 billion following the acquisitions of increased interests in TPS and ParisTV Câble) and the Energy sector (various acquisitions made by Tractebel in an amount of EUR 0.17 billion).

In 1998, **the Group share of return on equity,** calculated on the basis of average shareholders' equity was as follows:
- before amortization of goodwill: 13.5% (9.5% in 1997)
- following amortization of goodwill: 12.2% (8.5% in 1997)

Net consolidated debt amounted to EUR 10.65 billion, compared to EUR 9.21 billion as of December 31, 1997. This increase is primarily a result of the reclassification of the leasing contracts as from January 1, 1998, and the acquisitions of Gerasul and the BFI entities. The debt equity ratio was 59% as of December 31, 1998. Excluding the financial sector, gross operating income was over 7.5 times higher than net interest expense.

BREAKDOWN OF BUSINESS ACTIVITIES

(the composition of the Group's business sectors is set out in detail in Note 27)

In millions of EUR

	1998	Consolidation impact	Exchange rate impact	Net change	1997	% net change
Energy	10,766.8	664.4	(53.1)	399.2	9,757.2	4.1%
Water	5,119.7	62.0	18.9	307.0	4,730.9	6.5%
Waste services	5,119.8	1,232.6	(1.2)	427.2	3,461.2	12.3%
Communications	409.6	4.3	(0.3)	33.3	372.3	9%
Core businesses	**21,415.9**	**1,963.3**	**(35.6)**	**1,166.7**	**18,321.6**	**6.4%**
Retail financial services	2,436.8	(351.9)	(2.1)	(105.6)	2,896.4	-3.6%
Construction	6,878.8	(41.2)	(34.0)	314.2	6,639.8	4.7%
Other business lines	629.0	(483.4)	(1.7)	(57.5)	1,171.6	-4.9%
Others	**9,944.6**	**(876.4)**	**(37.8)**	**151.1**	**10,707.7**	**1.4%**
Group total	**31,360.5**	**1,086.9**	**(73.5)**	**1,317.8**	**29,029.3**	**4.5%**

Core businesses:

Interest rates had no material impact on the increase in revenues.

Energy:

Tractebel: revenues amounted to EUR 8,634.6 million, i.e. a net increase of EUR 306.6 million. The development of foreign business resulted in the addition of Almaty Power (Kazakhstan), Gerasul (Brazil), San Gabriel (California) and West Windsor (Canada) to the consolidated subsidiaries.

Elyo: revenues amounted to EUR 1,891.4 million in 1998 which was marked by the start-up of the Novergie group's major waste recovery plants in partnership with Sita and by the development of the Management-Maintenance business.

Lyonnaise des Eaux de Casablanca's (Morocco) share of business relating to electricity distribution is included in this sector for an amount of EUR 240.7 million generated over 12 months of activity compared to five in 1997.

Water:

Water distribution in France (40% of the sector's business, up 2%) was marked by sustained commercial activity, particularly in the area of sewage disposal.

In addition, this sector was boosted by the consolidation of Lydec (Morocco) over 12 months and the addition of Palyja (Indonesia) and United Water Services (United States) with a result that, on the international market, amounted to EUR 2,207.2 million. There continued to be significant international development, especially in Argentina and the United Kingdom.

In the area of water treatment, the Degrémont group (+6.3%) confirmed its strong position on the international market (70% of its business) and consolidated its position, particularly in the area of water treatment for the industrial sector.

Waste services:

There was significant growth in this sector using similar consolidation and exchange rate bases (almost 12%). The share generated by the company on the international market (excluding

France and Belgium) increased from 29% in 1997 to 45% in 1998.

With the acquisition of BFI's subsidiaries located outside North America and the full consolidation of the Brazilian subsdiary VEA, the Sita group's revenues increased by EUR 1 billion.

The environmental division of Tractebel also experienced sustained growth (+35% and +17.2% using similar consolidation and exchange rate bases) due, in particular, to the acquisition of A & J Bull (United Kingdom).

Communications:

The cable business in France saw an increase in the number of subscribers (+6.7%). TPS, consolidated under the equity method, did not contribute to consolidated revenues.

Métropole TV's advertising revenues increased by 13.7% while its advertising market share increased from 17% to 18%. The share of audience of its TVchannel M6 (transmission by radio waves) increased by 0.2% in 1998 to 13.4%.

The Tractebel Group continued to develop its business activities in Belgium related to new technologies. These activities are performed by Worldcom SA (telephony), Codenet (telephony and virtual communications network) and Datatrak (mobile communications vehicle tracking network).

Others:

Retail financial services:

The change in this sector's revenues stems essentially from the disposal of activities. Thus, ISM and La Hénin Epargne Crédit only contributed for the first six months of the fiscal year (EUR 0.3 billion). Sofinco, in which the Group still has a 30% stake following its sale to Crédit Agricole in January 1999, was fully consolidated in 1998 (EUR 0.75 billion). La Hénin Vie's operating income fell as a result of the changes in its markets without this decrease impacting its gross operating margin.

Construction :

Groupe GTM (EUR 6.85 billion) continued to reduce the relative importance of construction business in favor of road construction (EUR 2.04 billion, +14%), engineering (+50%) and offshore business (+23%).

Industrial stakes:

The sole surviving entity in this sector is the Recticel group. As the securities were sold by Société Générale de Belgique at the beginning of July 1998, only the first half of 1998 is consolidated.

GEOGRAPHICAL BREAKDOWN OF ACTIVITIES

The share of revenues generated on the international market increased throughout the Group. In the core businesses, it made up 37% of total revenues in 1998 compared to 27% in 1997.

In millions of EUR

	1998			1997		
	FRANCE	BELGIUM	INTERNATIONAL	FRANCE	BELGIUM	INTERNATIONAL
Energy	1,304.1	6,692.1	2,770.8	1,244.9	7,034.0	1,478.3
Water	2,279.9	29.6	2,810.2	2,278 .1	21.0	2,431.8
Waste services	1,836.1	858.4	2,425.3	1,573.3	946.7	941.2
Communications	330.8	66.4	12.4	282.2	74.4	15.7
Core businesses	**5,750.9**	**7,646.4**	**8,018.7**	**5,378.4**	**8,076.2**	**4,867.0**
Retail financial services	2,194.8		241.9	2,730.1		166.3
Construction	3,724.2	325.9	2,828.7	3,701.6	646.1	2,292.1
Other business sectors	88.4	502.8	37.9	217.8	944.4	9.3
Others	**6,007.4**	**828.7**	**3,108.4**	**6,649.5**	**1,590.5**	**2,467.7**
Group Total	**11,758.3**	**8,475.1**	**11,127.1**	**12,027.9**	**9,666.7**	**7,334.7**

Revenues by geographical area can be broken down as follows:

In millions of EUR

	1998	1997	1996 PRO FORMA
France	11,758.3	12,027.9	11,726.8
Belgium	8,475.1	9,666.7	8,719.9
European Union	5,110.0	2,944.5	2,522.1
Other European countries	943.4	670.4	416.2
Asia and Oceania	1,491.7	1,015.3	801.0
Africa	899.9	800.1	457.5
Americas	2,682.1	1,904.4	1,762.8
TOTAL INTERNATIONAL SECTOR	**31,360.5**	**29,029.3**	**26,406.3**

A significant portion of the business in Europe (excluding France and Belgium) is generated in the United Kingdom (37%) and in Spain (18%). In addition, the Group's position in Germany, Luxembourg and the Netherlands (20%) has significantly increased as the result of Sita's acquisition of the BFI network. Tractebel's increase in business in Hungary (Dunamenti) and Groupe GTM's growth in Eastern European countries account for the increase in the revenues for other European countries.

The first-time consolidation of Tractebel's business in Kazakhstan (EUR 0.34 billion) largely accounts for growth in the Asia zone.

BREAKDOWN OF INCOME

Gross operating income (EBITDA), one of the profitability indicators used by the Group, is calculated as follows:

In millions of EUR

	1998	1997 PRO-FORMA
Operating income before depreciation allowances and provisions	5,610.6	5,699.8
Elements of investment income not linked to net debt	236.1	234.5
Current income of companies accounted for under the equity method	256.7	306.4
Other reclassifications	18.0	10.3
GROSS OPERATING INCOME	**6,121.4**	**6,251.0**

The core businesses made up 77.3% of the total in 1998 (compared to 69.3% in 1997) and increased by 9.3%. The increase in the energy sector was attenuated, in particular by the impact of maintenance expenses, of a non-recurring nature, in the electricity sector in Belgium (which were in fact covered by provisions).

Gross operating income generated by the retail financial services sector is provided for information purposes only, as the specific nature of the insurance business makes this indicator less relevant. The recovery of Groupe GTM is shown by the growth in the gross operating income of the construction sector.

In millions of EUR

	1998	1997
Energy	2,909.7	2,767.7
Water	1,149.9	1,083.6
Waste services	636.8	429.0
Communications	38.3	50.3
Core businesses	**4,734.6**	**4,330.6**
Retail financial services	1,130.1	1,487.9
Construction	437.8	396.4
Others	(181.1)	36.1
GROUP TOTAL	**6,121.4**	**6,251.0**

The Group share of net current income income corresponds to the Group's share in current income of both fully consolidated companies and those accounted for under the equity method, after tax and amortization of goodwill. It may be broken down by business sector as follows:

In millions of EUR

	1998	1997	1996 PRO-FORMA
Energy	193.6	133.2	84.9
Water	211.6	213.0	191.9
Waste services	62.2	54.7	35.1
Communications	(29.0)	(8.1)	7.8
Misc. not allocated	3.2	3.8	
Core businesses	**441.6**	**396.6**	**319.7**
Retail financial services	245.3	188.0	180.0
Construction	62.5	51.4	33.4
Others	13.3	(27.0)	(9.0)
GROUP TOTAL	**762.7**	**609.0**	**524.1**

The contribution made by the **core businesses** increased by 11.3%.

The contribution made by the **Water** sector remained stable despite the scheduled impact of the start-up of major contracts won in 1997 (Manila, Jakarta). The drop in contributions made by the Degrémont and Northumbrian groups and by the Malaysian subsidiaries offset the improved profitability of the French water sector companies.

The contribution of the **Energy** sector was up by 45.3%. This results from the increase in the Group's share in Société Générale de Belgique and thus in Tractebel (with the minority interest increasing from 31% to 40% on average during the fiscal year) and by the development of the electricity and gas business on the international market (in Brazil and Kazakhstan, in particular). Furthermore, the Elyo group confirmed its turnaround in profitability.

The **Waste Services** sector was up by 13.7%. The increased contribution made to this business sector by the Tractebel, Northumbrian and Agbar groups more than compensated for the slight diluting effect, during the first year of consolidation, of Sita's acquisition of the BFI group's activities located outside North America.

As expected, the **Communications** sector was affected by the Group's increased interest in TPS (satellite television) as well as by the costs inherent to the digitalization of Lyonnaise Câble's sites.

Amongst the **other businesses,** the EUR 245.3 million contribution made by **retail financial services** benefited from the favorable consequences of the link-up between Fortis and Générale de Banque as well as the Group's increase in its stake in Société Générale de Belgique. For its part, the **Construction** sector contributed EUR 62.5 million and Groupe GTM confirmed its turnaround in profitability, in both public works and work in specialized fields (offshore work and road construction).

The Group share of net extraordinary income amounted to EUR 242.3 million compared to EUR 2.8 million for the 1997 fiscal year.

The Group share of net capital gains on disposals was primarily composed of the net effect of the disposals of Saint Gobain and Fortis B securities, for EUR 367.4 million and EUR 203.2 million respectively.

These results were partly offset by depreciation, provisions and other extraordinary charges, primarily composed of provisions relating to emerging country risks (EUR 98.3 million), various restructuring costs (EUR 88.3 million, including EUR 45.4 million with respect to Eau France), amortization of unconsolidated securities (EUR 72.3 million), extraordinary amortization of goodwill (EUR 50.6 million), provisions booked for long-term commitments relating to landfill sites (EUR 27.4 million; see Note 1) and costs required in preparation for the changeover to the euro and the year 2000 (EUR 24.2 million).

CASH FLOW STATEMENT

Gross cash flow (EUR 3.66 billion excluding the financial sector) covers 1.2 times the tangible and intangible investments (EUR 3.12 billion).

Disposals of assets (EUR 3.15 billion excluding the financial sector) cover 83% of financial investments during the fiscal year (EUR 3.75 billion) not taking into account the impact of the public offer of exchange with regard to Société Générale de Belgique, which was an equity-financed transaction.

Overall, the Group retained a solid financial structure.

GROSS CASH FLOW

Excluding the financial sector, cash flow increased by almost 1.6% with growth of 2.6% in the core businesses.

In millions of EUR

	1998	1997	1996 PRO-FORMA
Energy	2,123.8	2,207.3	2,113.9
Water	764.5	676.9	686.0
Waste services	402.9	291.5	214.5
Communications	(0.1)	31.2	53.8
Core businesses	**3,291.1**	**3,206.9**	**3,068.2**
Financial sector [a]	487.7	1,056.6	813.8
Construction	345.8	325.5	243.8
Others	17.2	65.1	75.0
GROUP TOTAL	**4,141.7**	**4,654.1**	**4,200.7**

(a) The above-mentioned financial sector includes retail financial services as well as the real estate companies that are subsidiaries of financial institutions.

INVESTMENTS

(excluding financial investments in the financial sector)

Intangible investments for the fiscal year, which amouted to EUR 0.17 billion, focused on the core businesses.

Tangible investments increased, primarily in the Waste Services and Energy sectors. The Construction sector increased its overall level of investment compared to 1997 thanks to significant investments carried out in 1998 in the Offshore sector.

The main financial investments relate to Suez Lyonnaise des Eaux's public offer of exchange with regard to Société Générale de Belgique (EUR 3.93 billion) within the framework of the policy of refocusing on its core businesses and simplifying its structures and to the acquisitions made by the Sita group (subsidiaries of bfi for EUR 1.3 billion) and by Tractebel (particularly Gerasul in Brazil for EUR 0.85 billion).

In 1997, financial investments were largely focused on Tractebel's expansion in Chile, Kazakhstan and Thailand, Sita's development in France and Brazil and Suez Lyonnaise des Eaux's takeover bids for Elyo and Degrémont.

In millions of EUR

	1998		1997	
	TANGIBLES AND INTANGIBLES	FINANCIAL (*)	TANGIBLES AND INTANGIBLES	FINANCIAL (*)
Energy	1,353.8	1,494.1	1,010.4	618.0
Water	805.1	285.4	1,081.9	308.5
Waste services	406.9	1,535.8	277.3	177.9
Communications	122.6	139.8	90.4	1.1
Core businesses	**2,688.5**	**3,455.1**	**2,460.0**	**1,105.6**
Retail financial services	21.8		96.5	
Construction	318.8	113.3	238.2	130.4
Others	125.1	(**) 4,120.7	205.2	359.6
GROUP TOTAL	**3,154.2**	**7,689.1**	**2,999.9**	**1,595.5**

(*) Excluding the financial sector

(**)Including the public offer of exchange with regard to SGB in an amount of EUR 3.93 billion.

DIVESTMENTS

Disposals of assets carried out in 1998 reflect the refocusing policy that was announced by the Group and amounted to EUR 3.17 billion in 1998 (in disposal prices) following disposals of EUR 2.41 billion in 1997. They include, in particular, the disposal of:

- investments in unconsolidated subsidiaries and affiliates, worth EUR 2.04 billion, held in particular by Suez Lyonnaise des Eaux SA (securities of Saint Gobain, Instituto San Paolo di Torino and CCF), Société Générale de Belgique (Fibelpar), Tractebel (Fibelpar, SES and Sipex) and the capital investment subsidiary, Suez Industrie;
- and securities of previously consolidated subsidiaries worth EUR 0.93 billion, mainly corresponding to Fortis B (disposal of 2.6%), ISM, La Hénin Epargne Crédit and Recticel.

INTERNATIONAL DEVELOPMENT OF THE GROUP AND THE ECONOMIC CRISIS IN ASIA

The method of development employed by the Group in emerging countries primarily consisted of carrying out concession or BOT (Build-Operate-Transfer) projects. Such operations are economical in terms of shareholders' equity but involve significant commitments vis-à-vis public concession grantors and lenders.

The Group's investment policy for international projects is generally reflected by the following "standard profile":

- industrial operator role, implementation of management and audit, reporting and control procedures;
- 20%-30% interest in shareholders' equity;
- search for one or more local financial and industrial partners;
- search for one or more international financial partners (SFI, BERD, etc.) Recognized and respected by the local authorities and the international financial community and which bear the final political risk (convertibility, transfer, compulsory purchase order) and the broader risk (the concession grantor's failure to comply with his contractual commitments, the regulator's failure to comply with the regulatory framework that applies to the sector);
- setting-up of unsecured financing, in local currency if this is authorized by the local financial markets;
- contractual protection clauses such as the "dollarization" of tarifs, the right to review prices and investments, the prin-

ciple of a project's economic and financial equilibrium and the fixing of upper limits on performance bonds.

Within the context of its policy of diversifying risks and sources of financing, two investment vehicles have been set up for projects in the Water sector: Lyonnaise Asia Water Limited (LAWL) and Lyonnaise Latin America Water Corporation Limited (LYLAW). They make it possible to associate financial partners in developing major international operations.

The effects of the economic crisis in Asia have not significantly affected the level of business and the performances of the Group's subsidiaries operating in the Asia-Pacific Area.

Alongside these measures, the Group is pursuing a conservative policy in terms of booking provisions for risks related to emerging countries. As of December 31, 1998, the Group's share of provisions booked amounted to EUR 187.2 million.

FIVE-YEAR FINANCIAL SUMMARY

In millions of EUR

	1998	1997	1996 PRO FORMA	1996 REPORTED	1995	1994
1. Revenues	31,360.5	29,029.3	26,406.3	13,967.4	15,033.8	15,239.6
Incl. revenues generated abroad	19,602.2	17,001.9	14,679.5	5,461.3	6,745.0	6,595.3
2. Income						
- current [a]	2,431.9	1,988.5	1,492.2	625.7	526.7	509.5
- of the consolidated group	2,058.4	1,604.4	1,297.1	318.5	206.0	319.2
- net income, Group share	1,005.0	611.8	302.0	205.7	138.1	161.8
3. Gross cash flow	4,141.7	4,654.1	4,200.7	1,114.1	923.5	999.8
4. Physical and financial investments	10,887.4	4,718.4	6,231.4	2,657.6	1,467.8	1,525.1
5. Total shareholders' equity	18,046.2	17,253.9	16,398.2	4,629.9	4,162.6	4,237.2
6. Shareholders' equity, Group share	8,931.1	7,515.9	6,921.2	2,809.8	2,509.5	2,467.5
7. Figures per share (in EUR)						
- earnings per share [b]	7.41	4.92	2.43	3.46	2.38	2.85
- dividend distributed (proposed for 98)	2.70	2.29	2.18	1.83	1.75	1.75
8. Total average workforce	333,132	305,936	287,137	156,719	154,688	151,873
- fully consolidated companies	201,129	174,458	169,238	116,290	118,770	114,514
- companies consolidated using the proportional consolidation method	41,456	31,791	27,755	31,952	26,384	26,421
- companies accounted for by the equity method	90,547	99,687	90,144	8,477	9,534	10,938

In millions of FRF

	1998	1997	1996 PRO FORMA	1996 REPORTED	1995	1994
1. Revenues	205,711	190,420	173,214	91,620	98,615	99,965
Incl. revenues generated abroad	128,582	111,525	96,291	35,824	44,244	43,262
2. Income						
- current [a]	15,952	13,044	9,788	4,104	3,455	3,342
- of the consolidated group	13,502	10,524	8,508	2,089	1,351	2,094
- net income, Group share	6,592	4,013	1,981	1,349	906	1,061
3. Gross cash flow	27,168	30,529	27,555	7,308	6,058	6,558
4. Physical and financial investments	71,416	30,951	40,875	17,433	9,628	10,004
5. Total shareholders' equity	118,375	113,178	107,565	30,370	27,305	27,794
6. Shareholders' equity, Group share	58,584	49,301	45,400	18,431	16,461	16,186
7. Figures per share (in EUR)						
- earnings per share [b]	48.6	32.3	15.9	22.7	15.6	18.7
- dividend distributed (proposed for 98)	17.7	15.0	14.3	12.0	11.5	11.5
8. Total average workforce	333,132	305,936	287,137	156,719	154,688	151,873
- fully consolidated companies	201,129	174,458	169,238	116,290	118,770	114,514
- companies consolidated using the proportional consolidation method	41,456	31,791	27,755	31,952	26,384	26,421
- companies accounted for by the equity method	90,547	99,687	90,144	8,477	9 ,534	10,938

(a) Following reclassification of compulsory employee profit-sharing under payroll expenses

(b) Earnings per share are calculated on the basis of the average number of outstanding shares, net of treasury stock.

CONSOLIDATED FINANCIAL STATEMENTS

INCOME STATEMENT

In millions of EUR

	NOTE N°	DEC. 31, 1998	DEC. 31, 1997	VAR. DEC.98 /DEC. 97	1996 PRO FORMA
Revenues		**31,360.5**	**29,029.3**	**8.0%**	**26,406.3**
Sales of goods and services		29,037.8	26,109.8	11.2%	23,469.1
Operating income from the financial sector		2,322.7	2,919.5	-20.4%	2,937.2
Other income		**1,889.0**	**1,834.7**	**3.0%**	**1,730.1**
Other operating income		898.1	901.7	-0.4%	760.4
Income from mixed inter-municipal companies and joint operations		990.9	933.0	6.2%	969.7
Operating expenses		**27,638.9**	**25,164.3**	**9.8%**	**23,194.3**
Purchases and changes in inventories		7,043.1	6,318.6	11.5%	5,490.9
Interest and other financial sector expenses		909.5	1,046.3	-13.1%	1,281.0
Receipts on behalf of local authorities		840.0	831.9	1.0%	816.2
Taxes and related payments		738.5	513.9	43.7%	443.9
Salaries, wages and social security charges		7,660.6	7,075.0	8.3%	6,565.5
Other operating expenses		10,447.2	9,378.6	11.4%	8,596.8
OPERATING INCOME BEFORE DEP., AMORT. AND PROVISIONS		**5,610.6**	**5,699.7**	**-1.6%**	**4,942.1**
Net depreciation allowances and provisions		2,074.5	2,344.3	-11.5%	2,125.3
Net technical provisions for the insurance sector		736.8	1,064.1	-30.8%	927.5
OPERATING INCOME	4	**2,799.3**	**2,291.3**	**22.2%**	**1,889.3**
FINANCIAL INCOME (LOSS)	5	**-367.4**	**-302.8**	**-21.3%**	**-397.1**
CURRENT INCOME OF CONSOLIDATED COMPANIES		**2,431.9**	**1,988.5**	**22.3%**	**1,492.2**
Net capital gains on disposals of assets		846.1	561.5	50.7%	515.2
Net provisions and losses on amounts due on investments		-294.1	-294.4	-0.1%	-231.9
Other net extraordinary expenses		-372.4	-317.1	17.4%	-154.6
EXTRAORDINARY INCOME (LOSS)	6	**179.6**	**-50.0**	**459.2%**	**128.7**
Corporate income tax	7	-644.0	-531.1	21.3%	-486.8
Share in income of companies accounted for under the equity method	8	255.7	300.3	-14.9%	228.2
Contribution of companies sold	2				86.3
NET INCOME BEFORE AMORTIZATION OF GOODWILL		**2,223.2**	**1,707.7**	**30.2%**	**1,448.6**
Amortization of goodwill	9	-164.8	-103.3	59.5%	-151.5
Incl. Group share		-107.0	-76.4	-40.1%	-95.3
TOTAL NET INCOME		**2,058.4**	**1,604.4**	**28.3%**	**1,297.1**
Minority interests		1,053.4	992.6	6.1%	995.0
NET INCOME, GROUP SHARE		**1,005.0**	**611.8**	**64.3%**	**302.1**
Earnings per share (in EUROS)		**7.41**	**4.92**	**50.5%**	**2.43**

CONSOLIDATED CASH FLOW STATEMENT

In millions of EUR

	DEC. 31, 1998			DEC. 31, 1997		
	FINANCIAL SECTOR	OTHERS	TOTAL GROUP	FINANCIAL SECTOR	OTHERS	TOTAL GROUP
Cash at beginning of year	**(3,259.4)**	**2,942.9**	**(316.5)**	**(3,897.5)**	**4,551.2**	**653.7**
Exchange fluctuations	(1.1)	(14.3)	(15.4)	3.7	34.2	37.9
Changes in scope of consolidation and other changes (mergers, reclassification, etc.)	619.0	53.0	672.0	78.0	(473.1)	(395.1)
ADJUSTED OPENING CASH BALANCE	**(2,641.5)**	**2,981.6**	**340.1**	**(3,815.8)**	**4,112.3**	**296.5**
Total net income	284.8	1,773.6	2,058.4	71.8	1,532.6	1,604.4
Dividends received from companies accounted for under the equity method, less share of consolidated income	(104.7)	(64.2)	(168.9)	(88.7)	(97.6)	(186.3)
Net depreciation allowances and provisions	453.5	2,795.0	3,248.5	1,241.4	2,594.1	3,835.5
Net capital gains on disposals of assets	(163.4)	(854.5)	(1,017.9)	(171.1)	(547.8)	(718.9)
Other items with no impact on cash flow	17.3	4.3	21.6	3.2	116.2	119.4
Gross cash flow	**487.5**	**3,654.2**	**4,141.7**	**1,056.6**	**3,597.5**	**4,654.1**
Change in working capital from operating activities	644.2	391.3	1,035.5	(228.8)	(36.7)	(265.5)
Change in working capital other than from operating activities	(22.3)	53.4	31.1	(76.2)	99.4	23.2
Cash flow from current activities	**1,109.4**	**4,098.9**	**5,208.3**	**751.6**	**3,660.2**	**4,411.8**
Tangible and intangible investments	29.9	3,124.3	3,154.2	136.4	2,863.5	2,999.9
Financial investments	44.1	7,689.1	7,733.2	123.0	1,595.5	1,718.5
Other working capital requirements (decrease)	424.7	(77.4)	347.3	674.6	134.6	809.2
Disposals of tangible and intangible assets	8.4	202.9	211.3	59.0	193.9	252.9
Disposals of long-term investments	68.5	2,896.8	2,965.3	275.0	1,886.3	2,161.3
Cash flow from investment activities	**(421.8)**	**(7,636.3)**	**(8,058.1)**	**(600.0)**	**(2,513.4)**	**(3,113.4)**
Dividends distributed	128.2	1,045.8	1,174.0	1.5	824.3	825.8
Repayment of long-term debts	436.6	2,064.3	2,500.9	459.8	3,857.4	4,317.2
Inter-sector financing	621.8	(621.8)	0.0	605.1	(605.1)	0.0
Increase in long-term debts	248.2	3,508.3	3,756.5	357.3	2,612.1	2,969.4
Treasury stock movements		(64.8)	(64.8)		(86.2)	(86.2)
Increase in total shareholders' equity	14.8	3,903.6	3,918.4	(96.2)	444.7	348.5
Cash flow from financing activities	**320.0**	**3,615.2**	**3,935.2**	**404.9**	**(2,316.2)**	**(1,911.3)**
TOTAL CASH FLOW FOR THE FISCAL YEAR	**1,007.6**	**77.8**	**1,085.4**	**556.5**	**(1,169.4)**	**(612.9)**
CASH AT YEAR-END	**(1,633.9)**	**3,059.4**	**1,425.5**	**(3,259.3)**	**2,942.9**	**(316.4)**

The cash position comprises the following items:

In millions of EUR

	AS OF DEC. 31, 1998	AS OF DEC. 31, 1997
Interbank transactions and securities in pawn, assets	586.9	724.7
Marketable securities	2.2	4.9
Interbank liabilities [(a)]	(2,023.0)	(3,105.0)
Inter-sector cash and related accounts	(200.0)	(883.9)
Financial sector	**(1,633.9)**	**(3,259.3)**
Cash and cash equivalents	2,827.9	2,079.4
Marketable securities	1,205.0	1,252.7
Bank overdrafts	(1,173.6)	(1,273.1)
Inter-sector cash and related accounts	200.1	883.9
Others:	**3,059.4**	**2,942.9**
TOTAL	**1,425.5**	**(316.4)**

(a) Falling due in less than three months

BALANCE SHEET - ASSETS

In millions of EUR

	Note N°	Dec. 31, 1998 Gross	Dec. 31, 1998 Dep, amort. & prov.	Dec. 31, 1998 Net	Dec. 31, 1997	Dec. 31, 1996 pro forma
Intangible assets	10.1					
Intangible rights on concessions		993.0	318.6	674.4	670.5	653.2
Other intangible assets		738.1	341.0	397.1	313.1	285.7
Goodwill	9	3,651.9	688.6	2,963.3	1,575.9	1,234.8
Tangible assets	10.1					
Owned outright	10.2	37,633.3	17,630.8	20,002.5	16,047.4	14,318.0
Under concession	10.3	6,693.3	1,886.7	4,806.6	4,798.6	4,345.6
Fixed assets in progress and down payments		1,023.4	3.8	1,019.6	894.4	593.0
Long-term investments						
Investments in subsidiaries	11	4,038.4	519.4	3,519.0	4,460.4	5,626.1
Financial sector investments	12	5,643.2	2.7	5,640.5	5,217.7	4,290.4
Companies accounted for under the equity method	8	5,717.8	13.2	5,704.6	5,665.9	5,286.3
Other long-term investments		1,417.0	196.2	1,220.8	1,126.6	769.5
TOTAL FIXED ASSETS		**67,549.4**	**21,601.0**	**45,948.4**	**40,770.5**	**37,402.6**
Inventories & work in progress	13	**4,187.3**	**139.8**	**4,047.5**	**4,580.5**	**4,699.9**
Accounts receivable						
Advances & down payments made on orders		78.5	0.0	78.5	64.2	61.6
Trade accounts and notes receivable		7,118.9	419.3	6,699.6	6,140.2	5,497.3
Other receivables		3,475.7	180.5	3,295.2	3,206.3	3,509.7
Financial assets						
Marketable securities	14	1,221.4	16.5	1,204.9	1,252.7	2,535.1
Cash and cash equivalents		2,827.9	0.0	2,827.9	2,079.6	2,166.3
Current assets in the financial sector						
Loans and credits		6,117.5	246.4	5,871.1	11,154.5	12,033.1
Interbank transactions and securities in pawn		984.7	11.0	973.7	1,574.0	2,700.9
TOTAL CURRENT ASSETS		**26,011.9**	**1,013.5**	**24,998.4**	**30,052.0**	**33,203.9**
Prepaid expenses	16	1,541.3		1,541.3	1,322.9	1,196.7
TOTAL ASSETS		**95,102.6**	**22,614.5**	**72,488.1**	**72,145.4**	**71,803.2**
Commitments received	22					

BALANCE SHEET - LIABILITIES

In millions of EUR

	NOTE N°	DEC. 31, 1998	DEC. 31, 1997	DEC. 31, 1996 PRO FORMA
Share capital		1351.6	1,154.6	
Additional paid-in capital		5,247.7	4,696.4	
Reserves		1,747.8	1,297.2	
Unrealized foreign exchange gains and losses	17.2	-186.0	-74.1	
Net income		1,005.0	611.8	
Treasury stock		-235.0	-170.0	
SHAREHOLDERS' EQUITY, GROUP SHARE	**17.1**	**8,931.1**	**7,515.9**	**6,921.2**
Minority interests	18	9,115.1	9,738.0	9,477.0
TOTAL SHAREHOLDERS' EQUITY		**18,046.2**	**17,253.9**	**16,398.2**
Special concession accounts*	19	4,243.3	4,248.3	3,795.8
Technical provisions for the life insurance sector	20.1	5,822.0	5,085.2	4,051.8
Other contingency & loss provisions	20.2	8,278.4	6,966.0	6,582.9
Borrowings & long-term debt	21	15,564.3	12,774.2	14,276.1
Accounts payable				
Advances and down payments received on orders		2,868.0	3,188.2	3,141.4
Trade payables		4,241.3	4,037.8	3,503.1
Other accounts payable		4,939.1	4,513.0	4,795.1
Miscellaneous liabilities				
On rights of use		322.4	333.6	362.4
Other miscellaneous liabilities		419.2	364.5	363.7
Total non-financial liabilities		**12,790.0**	**12,437.1**	**12,165.7**
Financial sector liabilities	15	5,897.5	11,523.9	12,858.9
Prepaid income	16	1,846.4	1,856.8	1,673.8
TOTAL LIABILITIES		**72,488.1**	**72,145.4**	**71,803.2**
* including counterpart of fixed assets received		3,343.7	3,368.7	3,004.5
Commitments given	22			

INCOME STATEMENT

In million of FRF

	NOTE N°	1998	1997	1996 PRO FORMA
Revenues		**205,711**	**190,420**	**173,214**
Sales of goods and services		190,475	171,269	153,947
Operating income from the financial sector		15,236	19,151	19,267
Other income		**12,391**	**12,035**	**11,349**
Other operating income		5,891	5,915	4,988
Income from mixed inter-municipal companies and joint operations		6,500	6,120	6,361
Operating expenses		**181,299**	**165,067**	**152,145**
Purchases and changes in inventories		46,200	41,447	36,018
Interest and other financial sector expenses		5,966	6,863	8,403
Receipts on behalf of local authorities		5,510	5,457	5,354
Taxes and related payments		4,844	3,371	2,912
Salaries, wages and social security charges		50,250	46,409	43,067
Other operating expenses		68,529	61,520	56,391
OPERATING INCOME BEFORE DEP., AMORT. AND PROVISIONS		**36,803**	**37,388**	**32,418**
Net depreciation allowances and provisions		13,608	15,378	13,941
Net technical provisions for the insurance sector		4,833	6,980	6,084
OPERATING INCOME	4	**18,362**	**15,030**	**12,393**
FINANCIAL INCOME (LOSS)	5	**(2,410)**	**(1,986)**	**(2,605)**
CURRENT INCOME OF CONSOLIDATED COMPANIES		**15,952**	**13,044**	**9,788**
Net capital gains on disposals of assets		5,550	3,683	3,379
Net provisions and losses on amounts due on investments		(1,929)	(1,931)	(1,521)
Other net extraordinary expenses		(2,443)	(2,080)	(1,014)
EXTRAORDINARY INCOME (LOSS)	6	**1,178**	**(328)**	**844**
Corporate income tax	7	(4,224)	(3,484)	(3,193)
Share in income of companies accounted for under the equity method	8	1,677	1,970	1,497
Contribution of companies sold	2			566
NET INCOME BEFORE AMORTIZATION OF GOODWILL		**14,583**	**11,202**	**9,502**
Amortization of goodwill incl. Group share	9	(1,081)	(678)	(994)
		(702)	(501)	(625)
TOTAL NET INCOME		**13,502**	**10,524**	**8,508**
Minority interests		6,910	6 511	6,527
NET INCOME, GROUP SHARE		**6,592**	**4,013**	**1,981**
Earnings per share (in FRF)		**48.6**	**32.3**	**15.9**

CONSOLIDATED CASH FLOW STATEMENT

In millions of FRF

	1998 Financial sector	1998 Others	1998 Total group	1997 Financial sector	1997 Others	1997 Total group
Cash at beginning of year	**(21,380)**	**19,304**	**(2,076)**	**(25,566)**	**29,854**	**4,288**
Exchange fluctuations	(7)	(94)	(101)	24	224	248
Changes in scope of consolidation and other changes (mergers, reclassification, etc.)	4,060	348	4,408	512	(3,103)	(2,591)
ADJUSTED OPENING CASH BALANCE	**(17,327)**	**19,558**	**2,231**	**(25,030)**	**26,975**	**1,945**
Total net income	1,868	11,634	13,502	471	10,053	10,524
Dividends received from companies accounted for under the equity method, less share of consolidated income	(687)	(421)	(1,108)	(582)	(640)	(1,222)
Net depreciation allowances and provisions	2,975	18,334	21,309	8,143	17,016	25,159
Net capital gains on disposals of assets	(1,072)	(5,605)	(6,677)	(1,122)	(3,593)	(4,715)
Other items with no impact on cash flow	114	28	142	21	762	783
Gross cash flow	**3,198**	**23,970**	**27,168**	**6,931**	**23,598**	**30,529**
Change in working capital from operating activities	4,225	2,567	6,792	(1,501)	(241)	(1,742)
Change in working capital other than from operating activities	(146)	350	204	(500)	652	152
Cash flow from current activities	**7,277**	**26,887**	**34,164**	**4,930**	**24,009**	**28,939**
Tangible and intangible investments	196	20,494	20,690	895	18,783	19,678
Financial investments	289	50,437	50,726	807	10,466	11,273
Other working capital requirements (decrease)	2,786	(508)	2,278	4,425	883	5,308
Disposals of tangible and intangible assets	55	1,331	1,386	387	1,272	1,659
Disposals of long-term investments	449	19,001	19,450	1,804	12,373	14,177
Cash flow from investment activities	**(2,767)**	**(50,091)**	**(52,858)**	**(3,936)**	**(16,487)**	**(20,423)**
Dividends distributed	841	6,860	7,701	10	5,407	5,417
Repayment of long-term debts	2,864	13,541	16,405	3,016	25,303	28,319
Inter-sector financing	4,079	(4,079)	0	3,969	(3,969)	0
Increase in long-term debts	1,628	23,013	24,641	2,344	17,134	19,478
Treasury stock movements		(425)	(425)		(565)	(565)
Increase in total shareholders' equity	97	25,606	25,703	(631)	2,917	2,286
Cash flow from financing activities	**2,099**	**23,714**	**25,813**	**2,656**	**(15,193)**	**(12,537)**
TOTAL CASH FLOW FOR THE FISCAL YEAR	**6,609**	**510**	**7,119**	**3,650**	**(7,671)**	**(4,021)**
CASH AT YEAR-END	**(10,718)**	**20,068**	**9,350**	**(21,380)**	**19,304**	**(2,076)**

The cash position comprises the following items:

In millions of FRF

	As of Dec. 31,1998	As of Dec. 31,1997
Interbank transactions and securities in pawn, assets	3,850	4,754
Marketable securities	14	32
Interbank liabilities [a]	(13,270)	(20,368)
Inter-sector cash and related accounts	(1,312)	(5,798)
Financial sector	**(10,718)**	**(21,380)**
Cash and cash equivalents	18,550	13,640
Marketable securities	7,904	8,217
Bank overdrafts	(7,698)	(8,351)
Inter-sector cash and related accounts	1,312	5,798
Others:	**20,068**	**19,304**
TOTAL	**9,350**	**(2,076)**

(a) Falling due in less than three months

BALANCE SHEET - ASSETS

In millions of FRF

	NOTE N°	DEC. 31, 1998 BRUT	AMORT. PROV.	NET	DEC. 31, 1997	DEC. 31, 1996 PRO FORMA
Intangible assets	**10.1**					
Intangible rights on concessions		6,514	2,090	4,424	4,398	4,285
Other intangible assets		4,842	2,237	2,605	2,054	1,874
Goodwill	**9**	23,955	4,517	19,438	10,337	8,100
Tangible assets	**10.1**					
Owned outright	10.2	246,858	115,650	131,208	105,264	93,920
Under concession	10.3	43,905	12,376	31,529	31,477	28,505
Fixed assets in progress and down payments		6,713	25	6,688	5,867	3,890
Long-term investments						
Investments in subsidiaries	11	26,490	3,407	23,083	29,258	36,905
Financial sector investments	12	37,017	18	36,999	34,226	28,143
Companies accounted for under the equity method	8	37,506	86	37,420	37,166	34,676
Other long-term investments		9,295	1,287	8,008	7,390	5,047
TOTAL FIXED ASSETS		**443,095**	**141,693**	**301,402**	**267,437**	**245,345**
Inventories & work in progress	**13**	**27,467**	**917**	**26,550**	**30,046**	**30,829**
Accounts receivable						
Advances & down payments made on orders		515		515	421	404
Trade accounts and notes receivable		46,697	2,751	43,946	40,277	36,060
Other receivables		22,799	1,184	21,615	21,032	23,022
Financial assets						
Marketable securities	14	8,012	108	7,904	8,217	16,629
Cash and cash equivalents		18,550		18,550	13,641	14,210
Current assets in the financial sector						
Loans and credits		40,128	1,616	38,512	73,169	78,932
Interbank transactions and securities in pawn		6,459	72	6,387	10,325	17,717
TOTAL CURRENT ASSETS		**170,627**	**6,648**	**163,979**	**197,128**	**217,803**
Prepaid expenses	16	10,110		10,110	8,678	7,850
TOTAL ASSETS		**623,832**	**148,341**	**475,491**	**473,243**	**470,998**
Commitments received	22					

BALANCE SHEET - LIABILITIES

In millions of FRF

	Note N°	Dec. 31, 1998	Dec. 31, 1997	Dec. 31, 1996 pro forma
Share capital		8,866	7,574	
Additional paid-in capital		34,423	30,806	
Reserves		11,465	8,509	
Unrealized foreign exchange gains and losses	17.2	(1,220)	(486)	
Net income		6,592	4,013	
Treasury stock		(1,542)	(1,115)	
SHAREHOLDERS' EQUITY, GROUP SHARE	**17.1**	**58,584**	**49,301**	**45,400**
Minority interests	18	59,791	63,877	62 165
TOTAL SHAREHOLDERS' EQUITY		**118,375**	**113,178**	**107,565**
Special concession accounts*	19	27,834	27,867	24,899
Technical provisions for the life insurance sector	20.1	38,190	33,357	26,578
Other contingency & loss provisions	20.2	54,303	45,694	43,181
Borrowings & long-term debt	21	102,095	83,793	93,645
Accounts payable				
Advances and down payments received on orders		18,813	20,913	20,606
Trade payables		27,821	26,486	22,979
Other accounts payable		32,398	29,604	31,454
Miscellaneous liabilities				
On rights of use		2,115	2,188	2,377
Other miscellaneous liabilities		2,750	2,391	2,386
Total non-financial liabilities		**83,897**	**81,582**	**79,802**
Financial sector liabilities	15	38,685	75,592	84,349
Prepaid income	16	12,112	12,180	10,979
TOTAL LIABILITIES		**475,491**	**473,243**	**470,998**
* including counterpart of fixed assets received		21,933	22,097	19,708
Commitments given	22			

NOTE 1 - ACCOUNTING PRINCIPLES AND VALUATION METHODS

Basis used:

The consolidated financial statements are drawn up within the framework of the provisions of the laws and regulations currently in force in France.

A. Consolidation principles

Fully consolidated companies and consolidation criteria:

The consolidated financial statements include, using the full consolidation method, the accounts of all of the significant subsidiaries over which Suez Lyonnaise des Eaux directly or indirectly exercises exclusive legal or de facto control. De facto control may result from contractual agreements or from exercising the majority of the votes at the company's General Meetings. Exclusive control may be deemed to exist where the direct or indirect shareholding exceeds 40% of the voting rights.

Companies which are jointly controlled by two or more shareholders are consolidated on a proportional basis, according to the percentage of control.

Companies over which Suez Lyonnaise des Eaux exercises a significant influence, which is presumed where the shareholding exceeds 20% of the capital, are accounted for under the equity method.

The list of the main consolidated companies is set out in Note 27.

Goodwill:

When a newly-acquired company is consolidated for the first time, any difference in value between the share in the company's net worth and the cost of acquisition that cannot be attributed to the appropriate items of the consolidated balance sheet, is recorded in the assets under "goodwill" if positive. If negative, it is recorded in the liabilities under "contingency and loss provisions."

Goodwill is amortized or written back to income over a maximum of 20 years except in the case of companies in France holding concessions for which goodwill generated since 1990 is amortized over a period of 40 years in view of the nature of their business.

In the event of significant adverse changes in the elements used to calculate the amortization and depreciation schedules, an extraordinary depreciation charge is booked.

Goodwill amortization is shown in a separate caption of the income statement. Amortization of goodwill is booked as an extraordinary expense in the income statement.

Intra-Group transactions:

Income and expenses, amounts receivable and payable and corresponding transactions recorded between fully consolidated companies are eliminated. If a given company is consolidated using the proportional method, elimination is carried out at the percentage of consolidation.

Where intra-Group transactions have a significant impact on net income, as in the case of capital gains on disposals of fixed assets, the resulting gain or loss is eliminated regardless of the method of consolidation of the companies in question. However, if the transaction carried out leads to an internal capital loss, a loss provision is set aside for the value of the asset sold if this can be justified. Capital gains or losses realized on transactions carried out with a company accounted for under the equity method are eliminated on the basis of this company's percentage stake.

Intra-Group provisions (on securities, debts and contingencies) are eliminated if duplicated in the cumulative net income of the consolidated company incurring the loss used for consolidation purposes. Otherwise, they are reclassified as contingency provisions.

Treasury stock:

Suez Lyonnaise des Eaux shares held by the parent company or by companies that it controls are deducted from net equity at their acquisition price. Dividends received on these securities are deducted from dividends distributed and the capital gains or losses made on disposals, net of tax, are allocated to additional paid-in capital.

Treasury stock held by proportionally-consolidated companies is eliminated in accordance with the percentage of consolidation.

B. Foreign currency translation methods

1. Translation of transactions in foreign currencies.

Amounts receivable and payable in foreign currency are translated at year-end exchange rates. Income, expenses and transactions are carried at the rate in force when they were posted.

2. Translation of the financial statements of foreign companies.

- **Balance sheet items** are translated into French francs at official year-end exchange rates. Shareholders' equity items are translated at historical rates; the difference in value resulting from changes in exchange rates compared with the previous year-end is included in unrealized foreign exchange gains and losses under shareholders' equity.

- **Income statement items** are translated at average exchange rates.

3. All of the data are then converted at the official rate of FRF 6.55957 for EUR 1, whether they relate to items in the balance sheet or in the income statement for the 1998 fiscal year or for previous fiscal years.

C. Intangible assets

In addition to start-up costs, intangible assets include:

- fees and amounts paid or payable in return for rights as the concession holder or operator of public sector facilities, amortized over the contract period.
- business goodwill, leasehold rights, patents and licenses are amortized over periods not exceeding their useful lives. Business goodwill is amortized over a maximum of 20 years.

Capital increase expenses are deducted from shareholders' equity.

Research and development expenses with no specific counterpart (contract, order) are booked as expenses.

D. Tangible assets

Tangible assets are stated at cost or, in the case of items which are subject to a legal revaluation, at their revalued amount, after deduction of accumulated depreciation. A distinction is made between:

- **assets owned outright**

These are assets owned by companies of the Group. They are valued and depreciated in accordance with standard practice in each sector. Infrastructures capitalized in the balance sheet of the English water subsidiaries are not depreciated. Expenses for renewal, major repairs and maintenance are stated as expenses and make it possible to maintain the production potential and thus the usefulness value of these assets.

- **assets under concession**

These consist of:

- assets placed under concession by the concession holder;
- assets provided free of charge by the grantor of the concession which the concession holder is under the obligation to renew. An equivalent value is recorded in the liabilities under the heading "special concession accounts."

The accounting principles that apply to concession items are set out in paragraph I.

In 1998, the Group adopted the principle of capitalizing assets either acquired by lease or those subject to similar contracts for all of its subsidiaries. Amounts outstanding with respect to the original value of these assets are booked as financial liabilities. The impact of this change in methods on net equity as of January 1, 1998 is set out in Note 17.

E. Investments in subsidiaries

These include:

- **Investments in unconsolidated subsidiaries and affiliates**

These represent long-term investments which are not consolidated but which make it possible to establish business relations with the issuing company or to take control of the issuing company or to exercise significant influence over it. These securities are booked at their acquisition value. Where applicable, such value is decreased by a loss provision, whose purpose is to reduce such value to its going value, which is estimated in particular by reference to the intrinsic value and financial return value.

- **Other long-term investments**

These are investments held in a long- or medium-term perspective, which do not correspond to the criteria set out for investments in unconsolidated subsidiaries and affiliates.

Amounts due from investments in subsidiaries make up the greater part of the "**other long-term investments**" item.

To ensure that financial income is of an equivalent nature to current income, and for the sake of year-to-year comparisons, as an exception to the General Chart of Accounts of 1982, all capital transactions relating to these three categories of assets have been recorded as extraordinary items. These notably concern allocations and reversals of provisions for investments and amounts due on investments in subsidiaries and, where applicable, writing off of these same provisions. For the sake of uniformity in presenting the income statement, these items are stated under extraordinary income and expenses, where gains and losses on disposals of securities are normally recorded. In 1998, this special treatment involved net reversals of EUR 143.5 million.

F. Financial sector investments

Financial sector investments represent medium- or long-term financial investments, held exclusively by the Group's financial institutions (insurance - banking) and carried out for the purpose of obtaining financial return.

With respect to insurance companies, some securities, notably those representing unit trust linked assurance contracts, are booked at the market rate. If necessary, a general loss provision may be set aside for other shares if the overall market value of the securities held is lower than the book value.

In the banking sector, a provision for losses is set aside for debt securities and bonds which are not intended to be held on a long-term basis (classified as "marketable securities" according to the General Chart of Accounts for the banking sector) where the market value of securities forming a homogeneous unit is lower than their book value. However, in relation to securities hedged by specific transactions, gains on hedging instruments are taken into account to calculate the provision to be set aside, where applicable. Shares are valued at cost, less a loss provision, calculated on a line-by-line basis, where their market value is lower than their book value.

G. Companies accounted for under the equity method

Companies accounted for under the equity method are reclassified, as necessary, in compliance with the Group's accounting principles. The Group's share in the reclassified net assets of these subsidiaries is included in assets on the balance sheet while its share of income is included on a specific line of the income statement.

Nonetheless, the following special treatment is applied to certain subsidiaries:

- Fortis B is one of the Fortis group's two parent companies which exercises its banking and insurance activities primarily in Belgium and the Netherlands. This group's accounting principles, which are in accordance with those generally applied in the Netherlands, are accepted by the Banking and Financial Commission in Brussels where the Fortis B securities are listed. In particular, Fortis constantly revalues its financial assets portfolio and allocates goodwill; this is offset by changes in consolidated shareholders' equity. The complete restatement of these principles would lead to the implementation of monitoring resources which would be disproportionate as to their cost, with no assurance of being able to obtain the required information within the time limits needed to produce the consolidated financial statements of the Suez Lyonnaise des Eaux Group. Consequently, the value of Fortis B accounted for under the equity method in the assets on the balance sheet corresponds to the share in shareholders' equity reported by Fortis B as of january 1, 1997 (date of processing of the merger between Suez and Lyonnaise des Eaux in the accounts) plus the share in income recorded each year by Fortis and less the amount of dividends received.

- mixed inter-municipal Belgian electricity and gas distribution companies: these companies are consolidated under the equity method by Electrabel. Association contracts and Belgian law give the local authorities in partnership with Electrabel a preponderant role in the management and monitoring of the activities, irrespective of the distribution of capital between the shareholders. Furthermore, in order to convey the importance and economic reality of this activity, Electrabel's share in the pre-tax income of these companies is included in operating income under the heading "income from mixed inter-municipal companies and joint operations".

H. Marketable securities

All of the listed marketable securities are valued at their closing market price. Any unrealized capital gain which may result from this is not booked.

I. Special concession accounts

These liabilities comprise:

- the counterpart of fixed assets received free of charge from the grantor of the concession and recorded in the company's assets under "tangible fixed assets." Depreciation calculated on these assets has no impact on income and is charged to this liabilities account;

- outside financing which may be provided to the concession holder for capital expenditures to be borne by it under the terms of the concession contract;

- amortization of assets under concession, for the purpose of rebuilding the funds invested by the concession holder (after deducting outside financing) in assets that must be returned free of charge to the grantor of the concession upon completion of the contract. This amortization is deducted from income over the residual life of the contract.

J. Contingency and loss provisions

Contingency provisions primarily concern:

- the reprocessing and storage of nuclear waste and future expenses relating to nuclear fuel reprocessing. These provisions are assessed on a contractual basis.

- the dismantling of nuclear units: such provisions are based on the estimated cost of dismantling nuclear power stations, to be allocated over their lifetime. Such estimate is based on studies carried out in 1990 and 1995 and updated to take into account recently-acquired knowledge and the experience gained from the dismantling of several European nuclear stations since that time.

- losses on completion of long-term contracts and real estate transactions.

- risks of a political or economic nature inherent to emerging countries which exceed normal operating risks.

- risks relating to direct operations or to unconsolidated subsidiaries.

- exchange rate fluctuation exposure.

Loss provisions are intended to cover in particular:

- the obligation for companies holding concessions to renew installations. These provisions are calculated by estimating the cost of replacing the installations based on their usefulness value, applying a present-value factor each year, using inflation as the basis of calculation. Insofar as the lifetime of fixed assets other than water pipes and mains is shorter than that of the contract, the provision is calculated line-by-line, spreading their replacement value over the lifetime of the asset in question. With regard to water systems, annual provisions are calculated contract-by-contract, with foreseeable partial replacement and repair costs spread over the life of each contract.

- major maintenance which is essentially intended to cover major repairs and servicing of both normal and nuclear power stations as well as gas production and transportation facilities. In addition, some companies in the Energy sector have a contractual commitment to maintain in serviceable condition or replace equipment forming part of installations covered by a "total warranty" clause. A provision is calculated on the basis of the present value of equipment and its lifespan when this is shorter than that of the contracts.

- site rehabilitation, and notably the contractual landfill rehabilitation commitment in the waste services sector. These provisions are calculated site-by-site, on the basis of the cost of repairs decided in proportion to the use of each site and after deduction of work already carried out.

- 30-year monitoring of landfill sites in the Waste Services sector, a long-term waste disposal site monitoring requirement that has been in effect in France since October 1998 and which will be extended to the other European Union countries once the European Parliament has finally passed the newly-introduced directive in this sector. The related provisions are calculated on a site-by-site basis and are set aside during the period of operation thereof. The costs which will have to be incurred during the 30-year period following closure of the site are discounted to present value. In 1998, the increase in these provisions resulting from the strengthening of the legislation was recorded as an exceptional expense.

- residual costs on completed projects in the Construction sector.

K. Bond discounts

Bond loans where repayment is accompanied by discounts are booked in the liabilities for their total value, including bond discounts. These discounts are, in return, recorded in the assets and amortized over the term of the loan in proportion to accrued interest.

L. Business activities and valuation of inventories

Revenues are calculated and inventories and work in progress are assessed in accordance with the rules applicable to each particular business sector existing within the Group.

The methods applied by individual companies are therefore reutilized for consolidation purposes.

• Electricity and gas production and distribution:

These activities are essentially carried out by Tractebel's Belgian subsidiaries (Electrabel and Distrigaz). The pricing practices, investments and dividends of these companies are regulated. Electricity and gas is distributed by mixed inter-municipal companies held by municipalities and by Electrabel. The contribution to consolidated business thus corresponds to the selling price invoiced by Electrabel to the mixed inter-municipal companies.

In order to illustrate the economic reality of this sector more fully in the consolidated financial statements, the income of the mixed inter-municipal companies, which relates to Electrabel's share in the profit margin on the distribution by these companies accounted for under the equity method, has been classified on a separate line within "operating income."

• Water distribution:

The booking of water sales includes all amounts billed to customers excluding value added tax, but including surtaxes and amounts collected on behalf of third parties as well as management expenses. The counterpart for sums collected in this way on behalf of local authorities is recorded on a separate line within "operating expenses." As far as management agreements are concerned, remuneration of the manager is recorded in services provided.

Sales of water are booked when meter readings are taken, which makes it possible to determine the amounts owed by the customers. If the water has not yet been delivered despite an invoice being issued in accordance with the contract (pre-billed subscriptions), a provision is booked at year-end on the balance sheet under the heading "loss provisions" for future delivery expenses incurred.

Inventories are composed of estimates of water delivered to customers but for which no meter readings have been made at year-end. These are estimated at cost by sub-groups of subscribers.

• **Construction:**

The Group applies the method of recognizing income in terms of percentage of completion. A provision is set aside for projects which seem certain to result in a loss on completion as soon as the loss is known. In estimating this loss, a percentage of potentially positive factors, notably additional invoicing and possible claims, may be taken into account. Determination of the quantity of such positive factors is carried out taking experience acquired in similar cases in the past into consideration. The research costs of projects in which tenders are being submitted at year-end are booked in "expenses to be accrued." A contingency provision is set aside for the total amount of such research.

• **Financial services (banks and insurance):**

All operating income (interest, insurance premiums, commissions, other financial income) is recorded as revenues. Management and financial arrangement commissions are booked as income at the date of collection or of completion of the transaction in question. Commissions on guarantees granted are booked in the income statement and prorated over the lifetime of the commitments or guarantees. Lease transactions are classified as loans and borrowings granted. Revenues from such transactions are included in income, after deduction of amortization calculated on a financial basis. Life insurance premiums are deemed to be acquired upon issue, irrespective of the period covered by the guarantee.

M. Deferred taxes

Deferred taxes arise from the neutralization of timing differences caused by tax regulations and consolidation adjustments. They are calculated annually, tax entity by tax entity, using the variable carry-forward method depending on the date when the difference will be reversed.

The net debit or credit position takes into account offsetting or imputations between deferred tax assets and deferred tax liabilities relating to different rates insofar as such offsetting or imputation of losses is regularly carried out in order to calculate the tax to be paid.

Suez Lyonnaise des Eaux has elected for tax consolidation treatment which incorporates most of its French subsidiaries in which it has an interest of over 95%. Consolidation treatment is taken into account to calculate deferred tax of companies consolidated for tax purposes.

Potential tax claims whose recovery is deemed uncertain are not booked.

There are deferred tax liabilities as of December 31, 1998, resulting essentially from accelerated tax depreciation of the tangible assets (excluding infrastructure) of British water distribution subsidiaries. The valuation carried out on the basis of projected investments (investments approved by the regulatory body OFWAT within the framework of a ten-year plan, and estimated very conservatively for subsequent years) shows that these deferred liabilities will only become payable in over 50 years time. Under such conditions, these deferred liabilities are not posted in the financial statements. They are included in off-balance sheet commitments.

N. Retirement indemnities and pension liabilities

According to the laws and customary practice of each country, group companies have obligations in terms of pension liabilities, early retirement, retirement indemnities and benefit plans.

These pension plan commitments and similar undertakings are subject to actuarial valuations where they represent clearly defined payments. Some companies within the Suez Lyonnaise des Eaux Group set aside provisions to cover their pension plan commitments as soon as reliable figures become available. In anticipation of its future compliance with standard IAS 19 in 1999 (which extends the concept of the provision for pension plan commitments to benefits other than pensions and to inter-company funds) and in accordance with the preferred methods recommended by the French National Accounting Institute, the Group is currently drawing up a list of its various commitments.

When it has been possible to make a reasonable estimate of the amounts relating to all these commitments, which are significant in character, quantified data will be provided and the necessary provisions will be booked by setting them off against shareholders' equity in light of the general application of the new standard.

O. Financial futures

Aside from the financial subsidiaries, which comply with regulations that are specific to their sector, financial futures transactions (purchases and sales of options and forward contracts) not yet closed out at year-end are recorded as follows:

- contracts on organized markets are marked to market;
- for over-the-counter (OTC) contracts, essentially interest rate swaps, the potential accrued interest differential is recorded.

Corresponding profits and losses are recorded as income in the same way as closed-out contracts, whose profits and losses are recorded for their net amount as interest income or interest expenses.

Assets and liabilities in the balance sheet directly or indirectly affected by these financial instruments are valued at year-end in accordance with the relevant accounting policies.

Contracts not yet closed out are recorded in the off-balance sheet commitments at their nominal value. They are set out in further detail in Note 22

P. Other items specific to the banking sector

Bank customer loans:

Loans to customers are stated in the balance sheet at nominal value and accrued interest is recorded in the income statement. A provision is set aside for unpaid interest and deducted from the assets while the unpaid interest is no longer recorded as income after 90 days or 180 days at the latest, depending on the type of business and the length of time for which the payment has been outstanding. Corresponding receivables are then classified as bad debts. Where changes to rates are granted due to the borrower experiencing financial difficulties, interest is booked in accordance with the new terms of the loan.

Provisions for bank customer loans are set aside in accordance with the estimated probable loss.

Funds for general banking risks:

In accordance with current regulations in the countries of the European Union, the general management of the Group's banks may decide to set up funds for general banking risks for reasons of conservatism in view of the risks inherent to bank transactions. Where hedging of identifiable risks results in the setting-up of such funds by banks belonging to the Group or is a consequence of such, these funds are stated in the liabilities of the balance sheet in "contingency and loss provisions." Otherwise, they are classified in the reserves and any changes to them have no impact on the income statement.

Leasing transactions:

Leasing transactions are classified as loans and credits granted. Revenues from these transactions are included in banking income, after deduction of depreciation calculated on a financial basis.

Q. Consolidated cash flow statement

This statement shows actual flows of funds associated with the operations of companies consolidated at year-end. The figures are thus based on an opening balance sheet restated for year-end exchange-rate and consolidation conditions. The effects on cash flow of changes in exchange-rate and consolidation conditions are set out at the beginning of the statement.

Nonetheless, where they are material, flows of funds relating to business between January 1 and their date of disposal by companies that have left the consolidated group during the fiscal year, are maintained in the cash flow statement.

Certain balance sheet movements are not considered to be flows, namely reclassifications, the impact of mergers and partial asset contributions, and changes in accounting methods.

Depreciation of current assets is classed as immediate realized losses. It thus has an impact on gross cash flow and has a counterpart in the flow resulting from current business based on changes in current assets, net of depreciation.

R. Earnings per share

Earnings per share are calculated in accordance with the average weighted number of shares that make up the outstanding capital during the fiscal year. Circulating shares are shares issued after deduction of treasury stock.

This number, and the earnings per share, is modified in order to take into account the possible impact of the dilution of shares to be issued within the framework of stock options, equity warrants and convertible bonds. However, if by taking into account such dilution the indicators per share are less than 5% higher or lower, the results of these calculations are not mentioned.

NOTE 2 - MAJOR ACQUISITIONS

2.1 Merger of Lyonnaise des Eaux and Compagnie de Suez

Accounting treatment of the merger operation:

The Annual General Meetings on June 11 and 19, 1997 approved the merger of Compagnie de Suez into Lyonnaise des Eaux, with retroactive effect as of January 1, 1997. This merger was recorded in the consolidated financial statements as follows (in millions of EUR):

NET ASSETS TRANSFERRED BY COMPAGNIE DE SUEZ, ACCORDING TO THE MERGER AGREEMENT	**4,916.3**
Corresponding consolidated net equity	5,097.5
Value adjustments to assets and liabilities	(144.1)
Elimination of intra-group goodwill	(691.4)
Other adjustments	(57.9)
Adjusted net equity	**4,204.1**
GOODWILL FROM THE MERGER, OFFSET AGAINST ADDITIONAL PAID-IN CAPITAL	**712.3**
Consolidated net equity of Lyonnaise des Eaux published as of December 31, 1996	2,809.8
Adjusted net equity contributed by Compagnie de Suez	4,204.1
Merger costs	(36.3)
Cancellation of items relating to treasury stock	(56.4)
Net equity contributed	**4,111.4**
NET EQUITY IN THE 1996 PRO-FORMA BALANCE SHEET	**6,921.2**

Contribution values

The assets and liabilities were booked in the parent company accounts of Lyonnaise des Eaux at their net values in the parent company accounts of Compagnie de Suez. These values became the cost of the assets in both the parent company accounts and consolidated financial statements of Suez Lyonnaise des Eaux.

The date of the operation is deemed to be January 1, 1997 (merger with retroactive effect). Thus, the following items, which did not give rise to payment at the time of the merger, were considered to have been carried out before the operation: the cancellation of Lyonnaise des Eaux and Suez securities held directly by Compagnie de Suez, the distribution of dividends carried out in June 1997 by Compagnie de Suez and the offsetting of all of the expenses connected with the merger, i.e. EUR 36.3 million, against additional paid-in capital. These last two operations are stated in the 1996 pro-forma balance sheet (see hereafter) in the prepaid income accounts.

Adjustment of the value of assets

The assets and liabilities of consolidated companies contributed by Suez were adjusted for the purposes of harmonizing accounting methods and due to the unrealized capital gains or losses calculated, for the listed securities, in accordance with their market value as of January 1, 1997. In view of the method used to book the above-mentioned contributions, the value of the assets and liabilities held directly by Compagnie de Suez was not adjusted.

Goodwill within consolidated sub-groups

This goodwill was eliminated in order to calculate a new difference at the level of the parent company. The Group share of goodwill amounted to EUR 691.4 million, almost all of which related to Société Générale de Belgique.

Offsetting of goodwill against additional paid-in capital

Following these various adjustments, the new goodwill amounted to EUR 712.3 million. It was offset against the additional paid-in capital. It was broken down with the aim of dividing it between the various underlying activities and is monitored to ensure that the proper treatment is applied, especially in the event of a disposal. If it had been booked in the assets and amortized over 20 years, the corresponding amortization expense would have amounted to EUR 35.7 million in 1997 and EUR 35.1 million in 1998.

Monitoring of accounting operations related to the merger in 1998

The valuation components taken into account for the treatment of the merger in 1997 were reexamined within the context of the accounts closing as of December 31, 1998. The opening balance sheet was not amended due to the insignificance of the variances noted.

Disposals of Recticel securities in early July 1998 and of Fortis B securities in late 1998 resulted in the booking, as a deduction from the capital gains, of part of the goodwill that was initially offset against additional paid-in capital (and additional paid-in capital related to the public offer of exchange with regard to Société Générale de Belgique - see paragraph 2.2 hereafter) in the amount of EUR 154.6 million.

Principles applied in order to draw up the pro-forma income statement and balance sheet as of December 31, 1996

Given the extent of the changes in the scope of consolidation which resulted from the merger, it appeared necessary to prepare 1996 pro-forma financial statements, in order to provide a more appropriate basis of comparison with the financial statements of the new unit for 1997 and 1998. The pro-forma income statement and balance sheet were drawn up as follows:

The consolidation method of certain companies was changed in relation to the previous practices of the Suez and Lyonnaise des Eaux groups to make a comparative review of the financial statements easier:

The companies consolidated in 1996, which were sold by either group in 1996 and 1997, were accounted for under the equity method and their contribution to the Group share of net income was reclassified on a separate line of the pro-forma income statement. Any capital gains or losses made at the time of disposal contribute to the extraordinary income for the period in question. This principle related mainly to Banque Indosuez, Factofrance Heller, Nevis Hotel Development, Société d'Epargne Viagère and Aquachem.

Tractebel and the Argentine water subsidiaries are fully consolidated while the investment retained in Union Minière is accounted for under the equity method.

The pro-forma income statement comprises the accumulated income statements of the two groups on the basis of the methods set out above. Only one adjustment entry is made to the Group share of net income: the share of Lyonnaise des Eaux's income due to Suez (following amortization of related goodwill), which amounted to EUR 32.2 million. Amortization of goodwill within the Suez group, which was subsequently canceled in order to draw up the opening balance sheet, therefore remains in the pro-forma income statement. The amount of such amortization amounts to EUR 70 million, of which EUR 35.4 million is the Group share. Adjustments to value also had no impact on pro-forma income. In 1996, no restatement was necessary with respect to the new Group's income as a result of transactions between the Suez and Lyonnaise des Eaux groups.

The pro-forma earnings per share is calculated using the number of shares circulating as of December 31, 1996 to which are added the number of shares resulting from the merger (66,226,733 shares).

By contrast, **the pro-forma balance sheet** was drawn up taking into account the accounting consequences of the merger: increase in capital and additional paid-in capital following the distribution of dividends by Compagnie de Suez, elimination of treasury stock, adjustment of the value of identifiable assets and liabilities and offsetting of goodwill against additional paid-in capital.

2.2 Public offer of exchange with regard to Société Générale de Belgique (SGB)

This public offer of exchange led to the contribution of 25,396,358 SGB shares paid for by the issue of the same number of Suez Lyonnaise des Eaux shares, noted by the Executive Board on July 2 and August 4, 1998. Suez Lyonnaise des Eaux's shareholding in SGB thus increased from 63.46% to 99.43%.

These contributions were also accompanied by the issue of 25,396,358 guaranteed value certificates (GVCs) entitling their holders to receive, between December 29, 2000 and March 30, 2001, a sum in French francs that is equal to the difference, if positive, between EUR 167.69 and the listed market price of Suez Lyonnaise des Eaux shares, as defined in the offer of exchange, up to EUR 27.44 per GVC.

Accounting treatment of the transaction:

This public offer of exchange was booked in the consolidated financial statements as follows (in millions of EUR):

Capital increase and additional paid-in capital representing the fair value of the SGB securities acquired	3,925.9
Share of SGB's consolidated equity acquired	(1,431.2)
Goodwill related to the transaction, offset against additional paid-in capital	2,494.7
Gross impact of the transaction on equity	1,431.2
Cancellation of internal capital gains realized on the exchange	80.9
Charging of expenses related to the transaction	(17.5)
Net impact of the transaction on equity, Group share	1,494.6

The share of equity acquired is valued on the basis of the shareholders' equity of the SGB group as of June 30, 1998. As Suez Lyonnaise des Eaux already controlled this company before the transaction, the value of SGB's assets was not adjusted.

The GVC is recorded in off-balance sheet commitments and will only be taken into account when booking the cost of the Société Générale de Belgique securities if it gives rise to a cash payment. The additional goodwill to be booked in this case would not be offset against equity but instead would be booked in the balance sheet and amortized over a period of 20 years.

Offsetting of goodwill against additional paid-in capital

The goodwill offset was broken down with the aim of dividing it between SGB's various underlying activities and is monitored to ensure that the proper treatment is applied in the event of any disposal.

If it had been booked in the assets and amortized over 20 years, the corresponding amortization expense would have amounted to EUR 59.2 million in 1998.

2.3 Acquisition of the Browning-Ferris Industries (BFI) group's activities outside North America

This acquisition, which took effect as of April 1, 1998, was made by Sita for a price of EUR 1.27 billion, taking into account a hedging option on the price of the USD which was entered into under favorable conditions. This acquisition was financed by way of a medium-term bank credit of approximately EUR 0.5 billion and equity in an amount of EUR 0.76 billion as follows:

- Increase in Sita's capital for an amount of EUR 0.41 billion to pay for a part of the assets contributed by BFI (Great Britain and New Zealand). This share issue enabled BFI to acquire a shareholding of 19.2%.
- Increase in Sita's capital in an amount of approximately EUR 0.35 billion in cash.

Following this transaction, Suez Lyonnaise des Eaux holds a 51.5% stake in Sita. As Suez Lyonnaise des Eaux did not issue securities in order to finance this transaction, the share of goodwill offset against additional paid-in capital in Sita's consolidated financial statements was rebuilt at the level of the Group's financial statements. The dilution gain resulting from this transaction was deducted from the goodwill rebuilt in this way. Consequently, the amount entered in the balance sheet in this regard is EUR 0.85 billion and will be amortized over 20 years (prorated over 9 months for 1998).

In addition, this transaction was accompanied by the signature of two agreements which included reciprocal put and call options:

- One between Sita and the Otto group relating to OED securities held by this German group,
- The other between Suez Lyonnaise des Eaux and BFI relating to the Sita securities held by BFI, including options which may be exercised under certain conditions (particularly, at the initiative of Suez Lyonnaise des Eaux in the event of substantial changes in the shareholding structure of BFI) and which will be closed out at market value.

The key figures in terms of contribution to the financial statements for the 1998 fiscal year (i.e. for 9 months in the income statement) are as follows (in billions of EUR):

Revenues	0.66
Operating income	0.06
Total balance sheet	0.67

2.4 Acquisition of Gerasul

In September 1998, within the framework of its energy sector deregulation program, the Brazilian government put up for sale its controlling interest in Gerasul. Through its IEG (International Electricity and Gas) division, Tractebel acquired 68.6% (and 77.3% of the voting rights) of Gerasul, which operates hydraulic and thermal power stations with power of 4,528 MW in the south of Brazil, supplying some 25 million people. The total investment amounted to BRC 1,195 million.

Gerasul's assets and liabilities were valued taking into account the impact of electricity sales agreements entered into with several suppliers before Tractebel became a shareholder, which run until 2005, within the context of the gradual movement from a regulated situation to a totally deregulated market in Brazil.

As a result, negative goodwill recorded in relation to these operations amounted to EUR 0.05 billion as of December 31, 1998.

The key figures in terms of contribution to the financial statements for the 1998 fiscal year (i.e. for 3 months in the income statement) are as follows (in billions of EUR):

Revenues	0.12
Operating income	0.06
Total balance sheet	3.31

NOTE 3 - CHANGES IN THE SCOPE OF CONSOLIDATION

The major changes to the scope of consolidation were:

First-time consolidation (fully consolidated unless otherwise stated):

Energy:

Gerasul (electricity production in Brazil: Tractebel group). See Note 2.4.

Almaty Power Cy, Intergas Central Asia and Global Gas Group (gas production and distribution in Kazakhstan: Tractebel group), H-Power (Thailand: Tractebel group), Gasoducto Nor Andino (Chile and Argentina).

Waste services:

Network of subsidiaries outside the United States, acquired by Sita from the BFI group. These companies are fully consolidated as from April 1, 1998. See Note 2.3.

A and J Bull (waste management, United Kingdom) in Tractebel's environmental division.

Water:

Palyja (water distribution in Jakarta, Indonesia)

Hager & Elsässer (water treatment engineering, Degrémont group in Germany).

Change in method:

West Windsor (Tractebel Inc. group in the United States), accounted for under the equity method in 1997 and now fully consolidated.

United Water Services (Lyonnaise des Eaux, water distribution in the United States), accounted for under the equity method in 1997 and now fully consolidated.

VEGA (Sita, Waste Services in Brazil), accounted for under the equity method in 1997 and now fully consolidated.

Deconsolidation:

Sita's Belgian subsidiaries were sold during the first half of 1998 to comply with the competition regulations set out within the framework of the BFI transaction.

La Hénin Epargne Crédit and ISM (retail financial services) were deconsolidated as of July 1, 1998 following their sale. The same applies to Recticel (polyurethane production).

Furthermore, Lydec (electricity and water distribution in Morocco) only contributed to the Group's financial statements for 5 months in 1997.

The impact of the changes in consolidation scope and methods on the financial statements, in millions of EUR, is as follows:

In millions of EUR

	NET IMPACT	EFFECT OF DECONSOLIDATION	EFFECT OF FIRST-TIME DECONSOLIDATION
Consolidation revenues	1,086.8	- 1,035.0	2,121.8
Current income (*)	14.6	- 57.8	72.4
Debt - net of cash flow (*)	1,129.3	- 309.2	1,438.5
Fixed assets	3,891.7	- 3,593.7	7,485.4

(*) Without taking into account the debt and financial expense which may have been incurred by the Group to finance acquisitions

NOTE 4 - OPERATING INCOME

Expenses relating to compulsory employee profit-sharing plans are classified under payroll expenses. In 1998 and 1997, they amounted to EUR 43 million and EUR 33.8 million respectively.

4.1 Other operating income:

In millions of EUR

	1998	1997
In-house production	320.9	235.8
Expense transfers (a)	222.7	286.9
Income from the sale of construction site equipment and assets under concession	33.5	28.5
Other current management income	321.0	350.5
TOTAL	**898.1**	**901.7**

(a) This heading includes capital increase costs offset against Suez Lyonnaise des Eaux additional paid-in capital for an amount of EUR 17.5 million in 1998 and EUR 36.3 million in 1997.

4.2 Income from mixed inter-municipal companies and joint operations:

In millions of EUR

	1998	1997
Share in mixed inter-municipal companies' income	909.3	867.7
Profits and losses transferred	81.6	65.4
TOTAL	**990.9**	**933.0**

Mixed inter-municipal companies' income corresponds to the share of Electrabel, Tractebel's subsidiary, in the income of mixed inter-municipal gas and electricity distribution companies in which it is associated with various Belgian municipalities.

4.3 Other operating expenses may be broken down as follows:

In millions of EUR

	1998	1997
Purchases not transferred to inventories	2,277.1	2,375.2
Sub-contracting	1,905.5	1,556.5
Rental and joint ownership expenses	649.9	558.3
External personnel	431.6	388.7
Repairs and maintenance	391.0	320.9
Intermediary fees and remuneration	345.6	272.0
Other external services	3,636.7	3,498.9
Miscellaneous	809.8	408.1
TOTAL	10,447.2	9,378.6

4.4 Operating income, interest and other financial sector costs

In millions of EUR

	Operating income		Interest and other costs	
	1998	1997	1998	1997
Gross insurance premiums written	748.8	1,020.8		
Interest and banking income	938.8	1,215.3		
Income from securities	407.3	404.9		
Income from rental of fixed assets	6.0	14.9		
Other operating income	221.8	263.6		
Insurance sector expenses			393.3	285.7
Interest and other bank charges			424.4	655.2
Interest on equity loans and subordinated notes			16.8	24.4
Bad debt losses			75.0	81.0
TOTAL	2,322.7	2,919.5	909.5	1,046.3

4.5 Net operating depreciation allowances and provisions are broken down as follows:

In millions of EUR

	1998	1997
Depreciation allowances	**1,934.5**	**1,775.3**
Intangible assets	160.2	151.7
Tangible assets [(a)]	1,716.1	1,575.6
Amortization of assets under concession	58.2	48.0
Provisions	**140.0**	**569.0**
For renewal of fixed assets	30.2	49.5
On current assets	63.1	22.1
For contingencies and losses [(b)]	(6.1)	468.5
Other	52,8	28.9
TOTAL	2,074.5	2,344.3

(a) Including, in 1998, depreciation allowance relating to leasing contracts: EUR 47 million.

(b) Having taken into account significant reversals of provisions booked in 1998 following the commitment of corresponding expenses (approximately EUR 0.3 billion, resulting primarily from withdrawals from real estate programs) and non-recurring allocations which affected the 1997 fiscal year (EUR 0.18 billion).

NOTE 5 - FINANCIAL RESULTS

Companies operating in the financial sector do not contribute to this item as the income and expenses that they record are included in operating income.

In millions of EUR

	1998	1997
Revenues from investments in subsidiaries and affiliates	253.7	219.4
Interest and similar expenses	(1,148.6)	(950.4)
Interest and equivalent income	437.7	334.6
Allowances to loss provisions on marketable securities	(29.4)	(20.9)
Other net financial revenues	119.2	114.5
FINANCIAL RESULTS	**(367.4)**	**(302.8)**

NOTE 6 - EXTRAORDINARY INCOME

6.1 Net capital gains on disposals of assets

The main disposals carried out during the fiscal year related to the securities of Saint Gobain (EUR 394.5 million), Fortis B (EUR 218.3 million), Société Européenne de Satellites (EUR 77.3 million) and Instituto San Paolo di Torino (EUR 32.5 million). The sale of La Hénin Epargne Crédit generated a capital loss of EUR 76.2 million.

6.2 Net allocations to provisions

In 1998, the Group's companies that are active in emerging countries (Asia, South America, Africa, Eastern Europe) continued the policy that was started in 1997 of booking provisions to cover risks related to setting up in these countries (EUR 170.3 million including EUR 98.3 million, Group share).

Some companies booked provisions for reorganization or restructuring costs, including EUR 45.4 million in the France Water division.

A EUR 23.5 million provision was booked for costs relating to the group's preparations for the changeover to the euro and for the year 2000, while expenses for the fiscal year amounted to EUR 10.5 million.

Extraordinary depreciation of non-financial assets amounted to EUR 106.4 million, including EUR 53.7 million in amortization of goodwill (EUR 30.5 million relating to the Elyo group).

Provisions for additional costs, related to new obligations to monitor landfill sites for 30 years after they cease being used, were booked for an amount of EUR 53.4 million in the Sita group (see Note 1.J).

6.3 Other extraordinary expenses

Other extraordinary expenses correspond primarily to restructuring (EUR 41.8 million) and costs associated with disposals of assets and winding-up of companies (EUR 196.1 million, over EUR 122 million of which was covered by previous provisions).

NOTE 7 - CORPORATE INCOME TAX

7.1 Income tax

In millions of EUR

	1998	1997
Taxes due on current income	(611.5)	(473.7)
Taxes due on extraordinary income	(27.9)	(7.6)
Deferred taxes on current income	(19.4)	(47.4)
Deferred taxes on extraordinary income	14.8	(2.4)
TOTAL INCOME TAX EXPENSE	**(644.0)**	**(531.1)**

French companies contributed 10% of the total corporate income tax expense.

Métropole Télévision, Groupe GTM and Sita are parent companies of tax consolidation groups, within the meaning of the provisions of Articles 223 A *et seq.* of the French Tax Code.

In 1998, Suez Lyonnaise des Eaux was the parent company of a tax consolidation group composed of 190 companies.

7.2 Deferred taxes

In millions of EUR

	ASSETS	LIABILITIES	NET LIABILITIES
AS OF DECEMBER 31, 1997	**230,8**	**530.8**	**300.0**
Changes in the scope of consolidation and unrealized foreign exchange gains and losses	64.3	(49.9)	(114.2)
Impact of the change in method applied to leasing transactions	14.3	0.0	(14.3)
Impact - income for the fiscal year	41.5	46.1	4.6
AS OF DECEMBER 31, 1998	**350.9**	**527.0**	**176.1**

Deferred tax liabilities resulted primarily from tax-regulated provisions booked in France and from the tax treatment of the depreciation of operating assets in the United States and Argentina. Provisions for pension plan liabilities resulted in a deferred tax asset of EUR 34.5 million.

NOTE 8 - COMPANIES ACCOUNTED FOR UNDER THE EQUITY METHOD

In millions of EUR

	1998		1997	
SHARE IN:	NET EQUITY	NET INCOME (LOSS)	NET EQUITY	NET INCOME (LOSS)
Core businesses	**3,431.6**	**6.7**	**3,329.8**	**30.6**
Belgian mixed inter-municipal companies	2,886.2	(a)	2,818.5	(a)
Other Tractebel subsidiaries	348.8	32.1	202.4	28.4
CEM (electricity company in Macao)	43.9	10.5	44.1	8.1
Malaysian water companies	29.4	2.9	28.4	5.8
Brazilian subsidiaries of Sita [(b)]			99.7	11.0
Télévision Par Satellite (TPS)	1.2	(42.8)	0.3	(24.9)
Other	122.1	4.0	136.4	2.3
Others	**2,273.0**	**249.0**	**2,336.1**	**269.7**
Générale de Banque [(c)]			989.6	117.6
Fortis B (banking and insurance) [(d)]	1,617.0	199.4	645.8	71.0
Union Minière (non-ferrous metals)	234.3	(12.2)	250.6	24.1
Groupe Cofiparco (motorway concessions)	205.5	46.7	186.5	41.5
Subsidiaries of GTM, parking facility management companies	101.5	13.1	98.8	9.9
Other	114.7	2.0	165.0	5.6
TOTAL	**5,704.6**	**255.7**	**5,665.9**	**300.3**

(a) Electrabel's share in the income of the mixed inter-municipal gas and electricity distribution companies is included in operating income (see Note 4.2).
(b) These companies are now fully consolidated.
(c) Générale de Banque was acquired by Fortis in 1998 and is now included in the contribution by this group.
(d) As of December 31, 1998, the market value of the Fortis B securities held by Société Générale de Belgique amounted to EUR 5.87 billion.

NOTE 9 - GOODWILL

In millions of EUR

	GOODWILL	NEGATIVE GOODWILL	NET
Goodwill as of December 31, 1997	**1,575.9**	**(20.1)**	**1,555.8**
Goodwill recorded in 1998	1,557.3	(81.5)	1,475.7
including:			
Acquisition of BFI's activities outside North America	858.8		
Acquisition of Tractebel's subsidiaries in Waste Services sector [(a)]	168.5		
Acquisition of Tractebel's subsidiaries in Energy sector [(b)]	161.9		
Changes in the scope of consolidation and unrealized foreign exchange gains and losses	58.3	0.6	58.9
Amortization expense	(174.4)	9.6	(164.8)
Extraordinary amortization [(c)]	(53.7)		(53.7)
BALANCE SHEET AS OF DECEMBER 31, 1998	**2,963.3**	**(91.4)**	**2,871.9**
GROUP SHARE	**2,018.7**	**(52.0)**	**1,966.7**

(a) Primarily, the increase in the Fabricom group's stake in Watco (wholly owned as of December 31, 1998).
(b) Includes goodwill related to the addition of H. Power, Intergas Central Asia, San Sabriel and West Windsor to the consolidated subsidiaries.
(c) Included in the income statement in extraordinary net amortization.

NOTE 10 - Fixed assets, depreciation and amortization

10.1 Tangible and intangible assets

Gross value

In millions of EUR

	As of December 31, 1997	Changes during year: Change in consolidation scope	Changes during year: Investments	Changes during year: Other changes (a)	As of December 31, 1998
Intangible assets	**1,661.2**	**115.6**	**167.3**	**(213.0)**	**1,731.1**
Owned outright	33,691.4	1,820.6	2,863.8	281.0	38,656.7
Under concession	6,510.5	(12.5)	123.1	72.3	6,693.3
Tangible assets	**40,201.9**	**1,808.0**	**2,986.9**	**353.2**	**45,350.0**

(a) including:

- disposals and eliminations — EUR (934.1) million
- among assets under concession, investments financed or contributed by third parties (local authorities, water authorities, etc.) — EUR 277.8 million
- effect of the change in accounting principle applied to leasing — EUR 787.1 million

Depreciation and amortization:

In millions of EUR

	As of December 31, 1997	Changes during year: Change in consolidation scope	Changes during year: Allowances	Changes during year: Other changes (a)	As of December 31, 1998
Intangible assets	**677.6**	**(44.7)**	**181.6**	**(154.9)**	**659.6**
Owned outright	16,749.6	(637.7)	1,726.5	(203.8)	17,634.6
Under concession	1,711.8	0.6	85.2	89.2	1,886.7
Tangible assets	**18,461.4**	**(637.1)**	**1,811.7**	**(114.7)**	**19,521.3**

(a) including:

- among assets under concession, depreciation recorded on behalf of concession grantors paid out of the special account for the counterpart of fixed assets received, included under liabilities in the balance sheet — EUR 166 million
- effect of the change in accounting principle applied to leasing — EUR 202.9 million
- disposals and eliminations — EUR (662.4) million

10.2 Tangible assets owned outright

In millions of EUR

	1998	1997
Land	464.1	350.0
Buildings	3,313.3	1,794.2
Machinery and equipment	11,500.6	9,358.2
Vehicles	500.2	378.1
Fixed assets under financial leasing (a)	895.2	1,317.5
Construction in progress and advance payments	1,019.6	894.4
Other fixed assets	3,329.2	2,849.4
TOTAL NET VALUE	**21,022.1**	**16,941.8**

(a) The variation in this item results from the change in the accounting principle applied to leasing (+ 459.3) and from the sale of subsidiaries (ISM, La Hénin Epargne Crédit, real estate subsidiaries) (- 1,111.8).

10.3 Tangible assets under concession

In millions of EUR

	1998	1997
Placed under concession by the concession holder	1,463.2	1,430.4
Placed under concession by the concession grantor	3,343.4	3,368.2
TOTAL NET VALUE	**4,806.6**	**4,798.6**

NOTE 11 - INVESTMENTS IN UNCONSOLIDATED SUBSIDIARIES AND AFFILIATES

The main investments in unconsolidated subsidiaries and affiliates are:

In millions of EUR

	1998		1997
	MARKET OR ESTIMATED VALUE	NET BOOK VALUE	NET BOOK VALUE
Pétrofina	983.1	668.8	669.1
Iberdrola	670.0	467.8	473.1
AXA-UAP	643.6	330.1	348.5
Scottish Power	302.7	164.9	165.0
Société Européenne des Satellites (S.E.S)	359.5	114.7	27.3
Powerfin GMBH	87.4	87.4	87.2
Acesa	227.8	77.4	77.6
Arbed	54.4	54.4	93.0
Compagnie de Saint-Gobain			457.0
Fibelpar			169.8
Other	2,193.5	1,553.5	1,892.8
TOTAL	**5,521.9**	**3,519.0**	**4,460.4**

Movements during the fiscal year may be broken down as follows:

In millions of EUR

AS OF DECEMBER 31, 1997	**4,460.4**
Acquisitions	673.1
Disposals, net book value	(1,355.1)
Net allocations to provisions	(68.9)
Changes in consolidation scope, exchange rate fluctuations and other changes	(190.4)
AS OF DECEMBER 31, 1998	**3,519.0**

The main acquisitions made during the fiscal year relate to the following investments: stakes acquired in Société Européenne de Satellites (S.E.S.) and Cégedel by Tractebel; stakes acquired in Bio Power and SHR by Elyo.

Disposals of securities primarily related to the following: Suez Lyonnaise des Eaux's interests in Saint Gobain, Instituto San Paolo di Torino and CCF; Société Générale de Belgique's and Tractebel's interests in Fibelpar; and Tractebel's interest in S.E.S.

NOTE 12 - FINANCIAL SECTOR INVESTMENTS

In millions of EUR

	1998	1997
Bonds	2,721.7	2,595.6
Shares	2,885.3	2,306.9
Treasury bonds		59.9
Negotiable debt securities	33.2	252.6
Related receivables	0.3	2.7
TOTAL NET BOOK VALUE	**5,640.5**	**5,217.7**

NOTE 13 - INVENTORIES AND WORK IN PROGRESS

In millions of EUR

	1998			1997
	GROSS	PROVISIONS	NET	NET
Raw materials	569.6	55.8	513.8	566.7
Work in progress	3,314.4	53.7	3,260.7	3,689.6
Finished products and goods	303.4	30.3	273.0	324.3
TOTAL	**4,187.3**	**139.8**	**4,047.5**	**4,580.5**

The change in work in progress should be considered alongside the change in down-payments received from customers on orders in the liabilities in the balance sheet.

NOTE 14 - MARKETABLE SECURITIES

The estimated value of the short-term investment securities portfolio as of December 31, 1998 amounted to EUR 1,241.7 million (i.e. an unrealized capital gain of EUR 36.7 million).

NOTE 15 - FINANCIAL SECTOR CURRENT ASSETS AND LIABILITIES

In millions of EUR

	CURRENT ASSETS		LIABILITIES	
GROSS	1998	1997	1998	1997
Inventories	37.7	370.5		
Loans and credits	5,871.1	11,154.5		
Other operating assets	347.1	473.9		
Interbank transactions and securities in pawn	586.8	724.7	2,025.9	3,220.0
Marketable securities	2.1	4.9		
Bonds, subordinated loans			989.9	3,033.7
Negotiable debt securities			2,446.4	3,690.2
Customer deposits			68.1	1,064.7
Other operating liabilities			367.3	515.3
TOTAL	6,844.8	12,728.5	5,897.5	11,523.9

NOTE 16 - ACCRUAL ACCOUNTS

In millions of EUR

	1998		1997	
	PREPAID EXPENSES & EXPENSES TO BE AMORTIZED	PREPAID INCOME	PREPAID EXPENSES & EXPENSES TO BE AMORTIZED	PREPAID INCOME
Prepaid expenses and accrued income	727.3		623.2	
Prepaid income and accrued liabilities		1,255.2		1,217.9
Deferred taxes	350.9	527.0	230.8	530.8
Expenses to be amortized	185.2		157.0	
Bond discounts to be amortized	109.8		125.8	
Unrealized foreign exchange gains and losses	9.5	18.8	6.8	11.3
Uncalled subscribed capital	16.2		23.8	
Other accruals	142.4	45.4	155.5	96.8
TOTAL	1,541.3	1,846.4	1,322.9	1,856.8

As of December 31, 1998, retail financial services contributed EUR 195.3 million to prepaid expenses and EUR 114.3 million to prepaid income (EUR 287.2 million and EUR 250 million respectively as of December 31, 1997).

NOTE 17 - SHAREHOLDERS' EQUITY

The changes in share capital as well as the outstanding marketable securities giving rights of access to capital are set out in the section of the annual report entitled "Legal and administrative information."

The number of shares shown in the table set out below corresponds to the number of outstanding shares before the elimination of treasury stock. As of December 31, 1998, the number of shares held by Suez Lyonnaise des Eaux or its subsidiaries was 2,643,824.

17.1 GROUP share of shareholders' equity

In millions of EUR

	Number of shares making up the capital	Capital	Additional paid-in capital	Consolidated reserves	Unrealized foreign exchange gains and losses	Treasury stock	Shareholders equity Group share
Shareholders' equity reported as of December 31, 1996	**59,315,239**	**542.6**	**1,259.2**	**1,193.7**	**(179.6)**	**(6.1)**	**2,809.8**
Merger with Cie de Suez	66,226,733	605.8	3,390.7	194.8		(79.9)	4,111.4
Pro-forma shareholders' equity as of December 31, 1996	**125,541,972**	**1,148.4**	**4,649.9**	**1,388.5**	**(179.6)**	**(86.0)**	**6,921.2**
Capital increases	693,800	6.4	46.5				52.9
Dividends distributed				(91.5)		2.3	(89.2)
Change in unrealized foreign exchange gains and losses					105.5		105.5
Miscellaneous						(86.3)	(86.3)
Income for the year				611.8			611.8
Shareholders' equity reported as of December 31, 1997	**126,235,772**	**1,154.8**	**4,696.4**	**1,908.8**	**(74.1)**	**(170.0)**	**7,515.9**
Public offer of exchange with regard to Société Générale de Belgique	25,396,358	232.2	1,157.7	104.7			1,494.6
Cancellation of shares	(4,759,580)	(43.6)	(686.3)				(729.9)
Conversion of bond loans	217,101	2.0	21.1				23.1
Conversion of stock options and employees' investment fund	678,086	6.2	55.0				61.2
Acquisition of treasury stock			3.8			(65.0)	(61.2)
Dividends distributed				(368.6)		4.6	(364.0)
Changes in unrealized foreign exchange gains and losses					(111.9)		(111.9)
Recovery of goodwill (*)				154.6			154.6
Change in method applied to leasing (**)				(47.9)			(47.9)
Miscellaneous				(8.3)			(8.3)
Income for the year				1,009.5		(4.6)	1,005.0
SHAREHOLDERS' EQUITY AS OF DECEMBER 31, 1998	**147,767,737**	**1,351.6**	**5,247.7**	**2,752.8**	**(186.0)**	**(235.0)**	**8,931.1**

(*) Goodwill offset against equity is recovered and deducted from the capital gain on disposals of assets when the companies in question are sold outside the Group. In 1998, the recovery resulted from the sale of Recticel and the sale of part of Fortis B.

(**) The change in accounting principle applied to leasing had the following effects on the financial statements in 1998:

On the balance sheet (value as of January 1, 1998):	
Gross value of fixed assets	787.1
Accumulated depreciation	(202.9)
Net book value	584.2
Debt	656.9
Deferred tax assets	15 .4
Effect on total shareholders' equity	(57.3)
Incl.: Group share	(47.9)

On the 1998 income statement:	
Depreciation and amortization	(47)
Cancellation of fee payment expenses	92.1
Financial expenses	(45.7)
Income from deferred taxes	0.3
Effect on total net income	(0.3)

17.2 Unrealized foreign exchange gains and losses

In millions of EUR

	DECEMBER 31, 1997	CHANGE	DECEMBER 31, 1998
Peseta	(80.8)	(1.1)	(81.9)
Dollar zone	(26.7)	(22.3)	(48.9)
Pound sterling	72.3	(54.7)	17.5
Belgian franc	(17.2)	(2.6)	(19.8)
Other currencies	(21.7)	(31.3)	(52.9)
TOTAL UNREALIZED FOREIGN EXCHANGE GAINS AND LOSSES	**(74.1)**	**(111.9)**	**(186.0)**

NOTE 18 - MINORITY INTERESTS

In millions of EUR

	1998	1997
MINORITY INTERESTS AS OF DECEMBER 31, 1996		**1,820.1**
Impact of merger with Compagnie de Suez		7,656.9
MINORITY INTERESTS AS OF JANUARY 1	**9,738.0**	**9,477.0**
Dividends distributed	(810.0)	(721.1)
Change in unrealized foreign exchange gains and losses	(81.7)	85.5
Income for the year	1,053.4	992.6
Changes in the consolidation scope [(a)]	(783.0)	(96.0)
Effect of reclassification of leasing	(1.7)	
MINORITY INTERESTS AS OF DECEMBER 31	**9,115.1**	**9,738.0**

(a) Includes minority shareholders' subscriptions to increases in the capital of consolidated subsidiaries (including BFI in the SITA group), the addition of the minority interests of newly-consolidated subsidiaries (including Gerasul, Tractebel's Brazilian subsidiary, for EUR 0.59 billion) and the buyback of the minority interests in Société Générale de Belgique via a public offer of exchange (EUR - 1.43 billion).

NOTE 19 - SPECIAL CONCESSION ACCOUNTS

In millions of EUR

	1998	1997
Third-party financing	311.8	344.8
Counterpart of fixed assets received from concession grantors	3,343.8	3,368.7
Amortization of assets under concession	587.7	534.8
TOTAL	**4,243.3**	**4,248.3**

NOTE 20 - CONTINGENCY AND LOSS PROVISIONS

20.1 Technical provisions for the insurance sector

Technical provisions for the insurance sector correspond to the difference between the current values of commitments made respectively by the insurer and the insured. In the case of contracts in currency units, this net commitment is restated at the fair market value of this currency unit at year-end.

20.2 Contingency and loss provisions

In millions of EUR

	1998	1997
Losses on completion and contractual commitments	506.4	146.1
Disputes, claims and tax risks	401.1	172.4
Foreign exchange losses	32.6	17.7
Sector-related risks	501.0	491
Risks relating to emerging countries [a]	303.7	133.4
Real estate risks [b]	505.2	786.6
Other risks	955.1	1,007.7
Total contingency provisions	**3,205.1**	**2,754.9**
Reprocessing and storage of nuclear waste	1,602.2	1,433.2
Dismantling of nuclear power stations	524.3	450.3
Major repairs and renovation	1,183.1	1,133.6
Warranty	245.3	227.6
Site rehabilitation	295.9	155.4
Pension liabilities	567.4	358.7
Project completion	62.1	64.6
Other expenses	501.6	367.6
Negative goodwill, net of amortization (see Note 9)	91.4	20.1
Total loss provisions	**5,073.3**	**4,211.1**
TOTAL CONTINGENCY AND LOSS PROVISIONS	**8,278.4**	**6,966.0**

(a) This item includes all provisions for country risks that are specifically devoted to geographical areas ordinarily classified as emerging countries. This definition covers the continent of South America, Asia (excluding Hong Kong, Macao and Singapore), Africa and Eastern Europe. The concept of country risk includes risks of a political or economic nature exceeding normal operating risks.

(b) This item includes all contingency liability provisions relating to the real estate sector whether these concern risks relating to real estate assets and receivables, losses on completion or risks relating to subsidiaries and sector-related risks. This item decreased following disposals of assets carried out in 1998.

NOTE 21 - FINANCING

21.1 MANAGEMENT OF FINANCIAL CONTINGENCIES

Cash management of the parent company and of the financial subsidiaries is centralized at the level of Suez Lyonnaise des Eaux. The main operating subsidiaries have their own organization but deposit the major part of their cash surplus with, or obtain financing for part of their short-term requirements from, the parent company.

Management of cash surpluses

Group cash surpluses are denominated almost entirely in euro zone currencies and do not therefore generate a foreign exchange risk. They are managed in order to generate maximum liquidity at minimum risk on the basis of reference to day-to-day exchange rates. In order to achieve these objectives, off-balance sheet financial instruments such as interest rate swaps or FRAs may be used within a framework laid down and approved by the Group's General Management.

Management of foreign exchange risks

The Group's policy is to systematically hedge exposure to foreign exchange risk generated by financial transactions denominated in a currency other than the national currency of the entity concerned. The foreign exchange risk related to long-term assets denominated in non-euro currencies is hedged when this is possible, through provision of financing in the same currency.

Debt management

Borrowings are, when possible, borne by operating companies in their cash flow currency; holding companies should not, by their nature, become indebted, except in exceptional circumstances. For the purpose of optimizing the structure and the cost of debt, the Group may carry out foreign currency or interest rate swaps. As of December 31, 1998, the Suez Lyonnaise des Eaux Group has a portfolio of confirmed, undrawn lines of credit amounting to EUR 1.84 billion.

Management of the counterparty risk

Transactions involving foreign exchange hedging, interest rate management or short-term investments are carried out exclusively using highly-rated counterparties approved by the General Management. These counterparties are chosen in line with the ratings assigned by credit rating agencies. The list thereof and the limit allocated to each counterparty is updated as and when necessary, in line with the change in ratings. Given the wide variety of counterparties used, the Group does not consider itself to be exposed to any concentration of its credit risk.

21.2 Breakdown of borrowings and long-term debt

BY CATEGORY

In millions of EUR

	1998	1997
Perpetual subordinated notes	186.5	228.7
Long-term debt	14,430.2	11,272.4
Bank overdrafts and cash current accounts	947.6	1,273.1
BORROWINGS AND LONG-TERM DEBT IN THE BALANCE SHEET	**15,564.3**	**12,774.2**

The perpetual subordinated notes were issued by Sofinco, Entreprise Jean Lefebvre and, for 1997, by La Hénin Epargne Crédit.

Changes in the consolidation scope and changes in consolidation methods resulted in a EUR 1.14 billion increase in debt while the impact of exchange rate fluctuations was a decrease of EUR 0.26 billion.

BY MATURITY DATE (EXCLUDING PERPETUAL SUBORDINATED NOTES AND OVERDRAFTS)

In millions of EUR

	1998			1997		
	< 1 YEAR	1 - 5 YEARS	> 5 YEARS	< 1 YEAR	1 - 5 YEARS	> 5 YEARS
Bond loans	531.3	660.6	1,791.4	98.3	1,395.7	1,676.0
Amounts due on bank loans	1,985.8	2,005.0	2,976.7	962.4	2,577.0	1,679.7
Leasing accounts	44.4	203.5	534.0			
Other borrowings and long-term debt	281.6	1,610.0	1,805.9	368.8	1,112.9	1,401.6
TOTAL	**2,843.0**	**4,479.1**	**7,108.1**	**1,429.5**	**5,085.6**	**4,757.3**

BY BUSINESS SECTOR

In millions of EUR

	1998		1997	
	GROSS	NET (d)	GROSS	NET
Core businesses:	**12,323.8**	**10,563.4**	**8,258.8**	**6,710.5**
Energy (a)	7,214.5	6,138.7	4,790.1	3,849.8
Water	3,781.7	3,294.7	2,961.2	2,495.7
Waste services	1,256.8	1,101.0	479.9	381.0
Communications	70.9	29.0	27.6	(16.0)
Construction	921.1	275.3	1,052.2	318.2
Other investments (b)	2,132.9	(189.5)	3,234.5	2,184.6
TOTAL (EXCLUDING PERPETUAL SUBORDINATED NOTES) (c)	**15,377.8**	**10,649.2**	**12,545.5**	**9,213.3**

(a) By agreement, all of the Tractebel group's debts are included in this sector

(b) The debts of Suez Lyonnaise des Eaux, Société Générale de Belgique and Crédisuez are included on this line

(c) Funding of the financial sector is not included in this item. It is broken down in Note 15

(d) Breakdown set out in paragraph 21.3.

21.3 Debt equity ratio

In millions of EUR

	1998	1997
Long-term debt	14,430.2	11,272.4
Bank overdrafts and cash current accounts	947.6	1,273.1
Marketable securities	(1,205.0)	(1,252.7)
Cash and cash equivalents	(2,827.9)	(2,079.6)
Hedged financial assets (*)	(695.8)	
Net debt	10,649.2	9,213.3
Total shareholders' equity	18,037.8	17,253.9
DEBT EQUITY RATIO	**59.0%**	**53.4%**

The reclassification of leasing, which was not carried out in 1997, contributed 4.3% to the increase in the debt equity ratio.

(*) These financial assets primarily relate to AXA securities booked at their net book value or at their value on sale if they have been hedged.

NOTE 22 - OFF-BALANCE SHEET COMMITMENTS

22.1 Surety bonds

As of December 31, 1998

In millions of EUR

	SURETY BONDS	
	GIVEN	RECEIVED FROM SUBCONTRACTORS
TOTAL	2,473.2	247.6

22.2 Guarantee commitments

These commitments primarily relate to guarantees given within the context of borrowings or credit lines taken out by non-financial companies within the Group or by financial institutions belonging to the Group within the scope of their banking activity.

As of December 31, 1998

In millions of EUR

	GUARANTEES	
	GIVEN (*)	RECEIVED
Financial sector	96.2	51.4
Others	2,792.4	201.7
TOTAL	2,888.6	253.1

(*) After deduction of the amount of borrowings already included in the consolidated balance sheet.

Furthermore, the Group's companies have pledged some of their assets in an amount of EUR 1,054.8 million as security for the repayment of their bank borrowings.

22.3 Commitments on interest rate, foreign exchange and stock markets

As of December 31, 1998

In millions of EUR

	FINANCIAL SECTOR	OTHERS
INTEREST RATE RISKS		
Off-balance sheet firm positions		
• Forward Rate Agreements (FRAs)		94.5
• Rate swaps	2,687.7	3,641.9
Off-balance sheet conditional positions		
• Caps	457.4	950.7
• Floors		166.2
• Collars		9.5
EXCHANGE RATE RISKS		
Off-balance sheet firm positions		
• Futures puts		559.6
• Futures calls		239.5
• Currency swaps		695.9
Off-balance sheet conditional positions (call and put options)		250.6
STOCK MARKET RISKS		
Off-balance sheet conditional positions		
• OTC agreements		(*) 777.2

(*) Primarily relates to put and call options regarding the AXA securities held.

22.4 Deferred taxes

The British subsidiaries of the Group have a deferred tax liability of EUR 184.9 million as of December 31, 1998, mainly relating to timing differences between the booking of depreciation for accounting and tax purposes on certain tangible assets (see Note 1 M). Over the coming years, the taxes due from these British subsidiaries will be decreased by EUR 95.9 million in line with the deduction of tax depreciation relating to other tangible assets held at closing.

22.5 Other commitments

Following the acquisition of Tractebel shares held by Electrafina and Royale Belge in late 1996, Société Générale de Belgique committed itself to purchasing Tractebel shares from other shareholders of this company willing to sell. This commitment was evidenced by 6,707,614 put warrants issued by Société Générale de Belgique and listed on the Brussels Stock Exchange, each entitling the holder to sell five Tractebel shares. The warrants are exercisable until November 1999 at a price of BEF 14,500 for 5 Tractebel shares, i.e. BEF 2,900 per Tractebel share; the Tractebel share market price as of December 31, 1998 was BEF 6,670. Out of all of the warrants issued, 1,273,204 are held by Société Générale de Belgique or by companies controlled by Société Générale de Belgique.

In 1998, guaranteed value certificates (GVCs) were issued to Suez Lyonnaise des Eaux shareholders who received these shares within the scope of the public offer of exchange with regard to Société Générale de Belgique's shares. The commitment corresponds to the entitlement of each of the 25,396,358 GVCs to receive, between December 29, 2000 and March 30, 2001, a sum in French francs equal to the difference, if positive, between EUR 167.3 and the listed Suez Lyonnaise des Eaux share price up to EUR 27.4 per GVC. As of December 31, 1998, the maximum amount of the commitment was EUR 696.8 million. At that date, the market value of the GVCs amounted to EUR 154.9 million.

As of December 31, 1998, the Tractebel Group undertook to contribute all of the Petrofina securities that it held to the Total group.

Within the context of the sales of businesses, the companies of the Suez Lyonnaise des Eaux Group are bound by seller's guarantee clauses for which provisions have been set aside when it seemed likely that they would be implemented.

As of December 31, 1998, the Group's financial sector entered into commitments to grant financing for an amount of EUR 4,854.4 billion.

The Suez Lyonnaise des Eaux Group gave other various commitments as of December 31, 1998 in a total amount of EUR 0.5 billion while other commitments received amounted to EUR 0.37 billion.

NOTE 23 - REMUNERATION OF CORPORATE OFFICERS

The figures shown hereafter represent the total remuneration received by the members of the Supervisory Board and by the members of the Executive Board and the corporate officers holding the positions listed on page 153 of this report.

In millions of EUR

	1998		1997 *	
	Number	Remuneration	Number	Remuneration
Supervisory Board	20	1.3	20	1.1
Members of the Executive Board and corporate officers	24	8.7	24	7.6

* The figures shown in the section "Members of the Executive Board and the Supervisory Board" for 1997 are based on the 1998 definition of corporate officers. The figures published in the 1997 report based on the definition of corporate officers existing at that time were respectively 21 corporate officers and EUR 7.42 million.

NOTE 24 - DISPUTES AND OTHER EXCEPTIONAL EVENTS

The Company is not aware of any dispute or other exceptional event liable to have a material impact on the business activities, results, financial position or assets of the Group which was not included in the consolidated financial statements as of December 31, 1998.

NOTE 25 - PREPARATIONS FOR THE CHANGEOVER TO THE SINGLE CURRENCY

The Group has prepared for the year 2000 date change by setting up an Executive Committee in June 1996, presided over by a member of the directorate, with the purpose of coordinating the Group's policy with respect to the year 2000 date change and to prepare for changeover to the single currency.

The Group Executive Committee has delegated responsibilities to the steering committees created within each of the Group's divisions and to the working groups set up in each subsidiary.

Plans for the year 2000 date change, which are drawn up company-by-company, are approved by the parent company of each of the Group's divisions. They take into account, not only management hardware and software, but also all the data processing and technical electronic equipment used by each of the Group's businesses. Any possible consequences for building management systems, including the impact on heating systems, elevators and control of access to the buildings themselves as well as the impact on automotive equipment, are also taken into account.

The most frequently used method takes place in five stages:

1. Inventory of programs, processes and equipment used
2. Evaluation of the critical nature of all equipment/facilities
3. Formulation of an action plan (changes, replacements, costs, timetable)
4. Devising and implementation of changes or replacements
5. Performance of validation tests (including with regard to suppliers).

Each division reports to the Group Committee on a quarterly basis. For the great majority of companies, the choice of new software and new hardware was made during the period; program configurations or modifications are in progress, in line with the approved timetable. The deployment phase for new software application packages and equipment has begun for the most part, and will be completed during the summer of 1999 or at the latest, in the fall.

In order to complete the measures taken, independent audits were carried out by an outside firm. In a number of isolated cases, they enabled corrective action to be taken or additional resources to be allocated.

Furthermore, each company is in contact with its main suppliers and subcontractors in order to obtain an assurance that they have implemented the necessary means to ensure continuity of supplies and services. Measures will be taken in order to avoid any disruption of supplies during this period.

Customer satisfaction is also a priority and all necessary measures will be taken to avoid customer problems at this time.

Finally, contingency plans will be implemented in order to deal with any incidents that may arise despite the preparations.

The consequences arising from the changeover to the single currency were handled in the same manner and priorities were assigned as follows:

- With effect from January 1, 1999, to provide amounts in both local currency and in euros on invoices and pay slips, to accept payments and to manage cash in euros. This first phase has been completed.
- To prepare for the changeover to the year 2000 for all management and data processing systems.
- Finally, to concentrate all our efforts on continuing the changeover to the euro in respect of all management and data processing systems.

Due to the complexity of the various systems and the interaction between them, the diversity of the Group's business lines, the simultaneous occurrence of changeover to the single currency and the year 2000 date change and the implications emanating from these issues, the Group is unable to separate costs involved in changeover to the year 2000 from those relating to changeover to the single currency.

In order to meet these two deadlines, the combined overall cost to the Group's companies is EUR 190 million, of which EUR 58.5 million has already been used. As of December 31, 1998, a provision of EUR 78.4 million was set aside for remaining expenses, relating to charges to be incurred.

NOTE 26 - EVENTS SUBSEQUENT TO THE CLOSING OF THE FINANCIAL YEAR

Sale of Sofinco

A sale agreement was entered into for the sale of Sofinco to Crédit Agricole, which was finalized on January 15, 1999. This transaction will take place in two stages:

In January 1999, Crédit Agricole acquired 70% of the capital of Sofinco:

- 18% through the exercise of a call option pursuant to the agreements entered into between the partners in August 1993,
- 52% by direct purchase.

In January 2000, the parties will be able to exercise reciprocal put and call options with regard to the balance of 30%.

The price of the 82% of the shares acquired other than by way of a call option was established on the basis of a valuation of Sofinco at EUR 1.58 billion. The total amount of the transaction was EUR 1.39 billion, valued as of December 31, 1998, and it should generate a pre-tax capital gain estimated at EUR 0.47 billion for the 1999 fiscal year and EUR 0.27 billion in the year 2000.

Issue of bonds with an option for exchange for AXA shares

On March1, 1999, Suez Lyonnaise des Eaux issued bonds in an amount of EUR 787 million with a maturity date of January 1, 2004. These bonds, with a nominal interest rate of zero, have a redemption cost upon maturity of 109.8% of their par value. The bearers hold an option with regard to the exchange of one share for one bond, which may be exercised against AXA shares between July 7, 1999 and December 24, 2003. In the event of this option being exercised, Suez Lyonnaise des Eaux would either have to sell, based on the issue price of the bonds, i.e. EUR 122 per share, 5.45 million AXA shares, or else pay the holders the difference between EUR 122 and the AXA share price on the date on which the option is exercised. Suez Lyonnaise des Eaux has the possibility to redeem the bonds early for an amount of up to a maximum of 50% of their value at the end of December 2001, or for the balance remaining at the end of December 2002. The bonds are listed on the Luxembourg stock exchange.

Early retirement of convertible 6.5% bonds (June 1990/January 2000).

On December 8, 1998, Suez Lyonnaise des Eaux announced the early redemption of convertible 6.5% bonds (June 1990/January 2000) from January 4, 1999 onwards, in accordance with the possibility outlined in the issue contract.

If the 2,893,412 outstanding convertible bonds remaining as of December 31, 1998 are converted, the debt will be reduced by EUR 0.38 billion.

Sale of La Hénin Vie

Suez Lyonnaise des Eaux and the mutual life assurance company La Mondiale announced on January 11, 1999 that they had reached an agreement on the acquisition by La Mondiale of a 68.3% stake in the capital of La Hénin Vie as well as the La Hénin Vie perpetual subordinated notes held by Suez Lyonnaise des Eaux.

The completion of this operation is subject to certain condition precedents including the carrying out by La Mondiale of an audit of the financial statements of La Hénin Vie as of December 31, 1998.

NOTE 27- LIST OF THE MAIN CONSOLIDATED COMPANIES AS OF DECEMBER 31, 1998

Core businesses

COMPANY NAME	ADDRESS OF REGISTERED OFFICE	% INTEREST 1998	% INTEREST 1997	CONSOLIDATION METHOD
ENERGY				
Tractebel (1) and (2)	Place du Trône 1 B - 1000 Brussels - Belgium	49	31	IG
ELECTRABEL (Tractebel group)	Boulevard du Regent, 8 - 1000 Brussels - Belgium	19	12	IG
DISTRIGAZ (Tractebel group)	Avenue des Arts, 31 - 1040 Brussels - Belgium	20	13	IG
ELYO	235, avenue Georges Clémenceau - 92000 Nanterre	100	99	IG
C.E.M. (Companhia de Electricidade de Macau)	Estrada D. Maria 11, Edificio CEM - Macao	12	12	ME
WATER				
LYONNAISE DES EAUX	72, avenue de la Liberté - 92753 Nanterre	100	100	IG
EAU ET FORCE	72, avenue de la Liberté - 92753 Nanterre	100	100	IG
EAUX DE MARSEILLE	25, rue Edouard-Delanglade - 13006 Marseille	49	49	IP
EAUX DU NORD	217, boulevard de la Liberté - BP 329 - 59020 Lille	50	50	IP
STEPHANOISE DES EAUX	28, rue Eugène Beaune - 42043 Saint-Etienne cedex	50	50	IP
S.C.M. (SDEI)	988, chemin Pierre Drevet - 69140 Rillieux-la-Pape	100	100	IG
DEGREMONT	183, avenue du 18 juin 1940 - 92500 Rueil-Malmaison	100	100	IG
UNITED WATER RESOURCES (3)	200 Old Hook Road, Harrington Park New Jersey - USA	29	26	IG
S.A.A.M. (Sociedad de Abstecimiento de Aguas de Macau)	82, avenue do Conselheiro - Borja PO BOX 115 - Macao	26	26	IP
NORTHUMBRIAN WATER	Regent Centre, Gosforth, Newcastle upon Tyne NE3 3PX - UK	71	71	IG
AGBAR (2)	Paseo de San Juan, 39, 08009 Barcelona - Spain	26	26	IP
EURAWASSER	Cicerostr. 26 - 10709 Berlin - Germany	50	50	IP
AGUAS ARGENTINAS	Reconquista 823, 1003 Buenos Aires - Argentina	42	28	IG
AGUAS PROVINCIALES DE SANTE FE	Cordoba 844, piso 5 Rosario 2000 - Argentina	56	36	IG
LYDEC	20, boulevard Rachidi, Casablanca - Morocco	60	60	IG
WASTE SERVICES				
SITA	132, rue des Trois Fontanots - 92758 Nanterre	51	64	IG
FABRICOM (Tractebel group) (1)	Rue de Gatti de Gamond, 254 - 1180 Brussels - Belgium	49	31	IG
NEM	Regent Centre, Gosforth, Newcastle upon Tyne NE3 3PX - UK	71	71	IG
CESPA	Henao, 20 entreplanta - Bilbao - Spain	46	46	IG
COMMUNICATIONS				
METROPOLE TV	89, avenue Ch. de Gaulle - 92200 Neuilly-sur-Seine	34	34	IP
CODITEL (Tractebel group) (1)	Rue des Deux Eglises, 26 - 1000 Brussels - Belgium	39	24	IG
LYONNAISE COMMUNICATIONS	20, place des Vins de France - 75614 Paris cedex 12	77	77	IG
AUXIPAR	20, place des Vins de France - 75614 Paris cedex 12	100	100	IG
TPS	145, quai de Stalingrad - 92137 Issy-les-Moulineaux	34	17	ME

IG = full consolidation - ME = equity method - IP = proportional method

(1) Shareholding in 1998 after the public offer of exchange with regard to Société Sénérale de Belgique carried out in July 1998.

(2) The data relating to these multi-activity groups are set out in detail by business sector in the management report. Tractebel's and Agbar's main consolidated subsidiaries are included on this list for information purposes.

(3) Potential shareholding of 32.8% following the conversion of preference shares held.

Others

COMPANY NAME	ADDRESS OF REGISTERED OFFICE	% INTEREST 1998	1997	CONSOLIDATION METHOD
CONSTRUCTION				
GROUPE GTM	61, avenue Jules Quentin - 92000 Nanterre	50	50	IG
DUMEZ-GTM	61, avenue Jules Quentin - 92000 Nanterre	50	50	IG
CHANTIERS MODERNES	18, avenue Gustave Eiffel - 33600 Pessac	50	50	IG
C.F.E.	Chaussée de la Hulpe, 164 - Brussels - Belgium	23	23	IG
ENTREPRISE JEAN LEFEBVRE	11, boulevard Jean Mermoz - 92202 Neuilly-sur-Seine	48	48	IG
ETPM	32, avenue Pablo Picasso - 92002 Nanterre	50	50	IG
INGEROP	168/172, boulevard de Verdun - 92413 Courbevoie	50	50	IG
DELATTRE LEVIVIER	Tour Fiat - 92084 Paris La Défense	50	26	IG
GTM H	72, rue Gabriel Péri BP 510 - 92542 Montrouge	50	50	IG
COFIROUTE	77, avenue Raymond Poincaré - 75116 Paris	33	33	ME
FINANCIAL SERVICES				
FORTIS B (1)	Boulevard E. Jacqmain, 53 - 1000 Brussels - Belgium	16		ME
BANQUE SOFINCO	Rue du Bois Sauvage - 91038 Evry	100		IG
LA HENIN VIE	14, rue Roquépine - 75379 Paris	88		IG
OTHERS INTERESTS HELD				
SOCIETE GENERALE DE BELGIQUE (1)	Rue Royale, 30 - 1000 Brussels - Belgium	100		IG
CREDISUEZ	1, rue d'Astorg - 75008 Paris	100		IG
COFICEM / SAGEM (SGB group) (1)	6, avenue d'Iéna - 75783 Paris cedex 16	20		ME
UNION MINIERE (SGB group) (1)	Rue du Marais, 31 - 1000 Brussels - Belgium	25		ME
SUEZ INDUSTRIE	68, rue du Faubourg Saint-Honoré - 75008 Paris	100		IG
REAUMUR PARTICIPATIONS	115, rue Réaumur - 75002 Paris	100		IG
FONCIERE DE L'ARCADE	115, rue Réaumur - 75002 Paris	100		IG
DUMINVEST	115, rue Réaumur - 75002 Paris	100	100	IG
DUFIMM	115, rue Réaumur - 75002 Paris	100	100	IG

(1) Shareholding in 1998 after the public offer of exchange with regard to Société Sénérale de Belgique carried out in july 1998.

STATUTORY AUDITORS' REPORT ON THE CONSOLIDATED FINANCIAL STATEMENTS

To the shareholders of Suez Lyonnaise des Eaux,

In compliance with the assignment entrusted to us at the Annual General Meeting of Shareholders, we have examined the accompanying consolidated financial statements of Suez Lyonnaise des Eaux for the period ended December 31, 1998.

These consolidated financial statements have been approved by the Executive Board. Our role is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with the professional standards applied in France. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management to draw up the financial statements, as well as evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements give a true and fair view of the Group's financial position, and its assets and liabilities, and of the results of operations of all the companies included in the consolidation scope.

Without qualifying the opinion expressed above, we wish to draw your attention to Notes D and N of the Notes to the Financial Statements which set out your Group's position in relation to the preferred methods recommended by the French National Accounting Institute in terms of leasing and retirement indemnities and pensions.

We also performed the verification of the information relating to the Group given in the management report. We have no comments to make as to its fair presentation and its conformity with the consolidated financial statements.

Neuilly-sur-Seine and Paris, April 16, 1999

The Statutory Auditors

Barbier Frinault & Autres
Arthur Andersen
Christian Chochon

Mazars & Guérard
Frédéric Allilaire

Allilaire.

PARENT COMPANY ACCOUNTS

INCOME STATEMENT

In millions of EUR

	Note No.	1998	1997	1996 PRO FORMA	1996 REPORTED
Operating income		**1,320.2**	**1,299.6**	**1,213.4**	**1,210.6**
Revenues		1,182.9	1,163.0	1,113.9	1,113.9
Finished goods & in-progress inventory		4.8	0.8	13.5	13.5
In-house production		34.1	33.5	33.2	33.2
Operating subsidies		5.2	3.4	3.5	3.5
Reversals of provisions, amortization & depreciation and expense transfers		91.1	95.8	44.6	42.6
Other operating income		2.2	3.1	4.8	4.0
Operating expenses		**1,352.9**	**1,276.8**	**1,188.2**	**1,151.1**
Purchases of raw materials and other supplies		20.0	19.0	19.6	19.6
Changes in inventories		(0.5)	(0.3)	(0.3)	(0.3)
Other purchases and external charges		422.4	387.1	331.5	316.4
Management costs and fee payments		394.5	387.2	378.4	378.4
Taxes and related payments		29.0	28.1	28.2	23.9
Payroll expenses		293.7	290.2	279.4	266.9
Depreciation allowances & provisions		173.3	151.3	141.4	136.4
Fixed assets: depreciation allowances		87.5	85.9	83.1	80.0
Fixed assets: provisions		42.7	43.5	45.1	45.1
Current assets: provisions		6.5	4.6	4.3	4.3
Contingencies and losses: provisions		36.6	17.2	8.9	7.0
Other operating expenses		20.5	14.3	10.1	9.7
OPERATING INCOME (LOSS)	2	**(32.7)**	**22.8**	**25.2**	**59.5**
Share of income from joint operations		**0.2**	**(4.3)**	**(0.6)**	**(1.3)**

INCOME STATEMENT

In millions of EUR

	NOTE NO	1998	1997	1996 PRO FORMA	1996 REPORTED
Financial income		**618.3**	**633.8**	**533.9**	**218.8**
Income from investments in subsidiaries and affiliates		525.1	515.9	450.9	163.1
Income from other marketable securities and non-current loans and advances		16.3	12.4	20.5	0.7
Other interest and related income		42.9	35.0	41.8	38.2
Reversals of provisions and expense transfers		3.5	3.3	3.3	3.2
Foreign exchange gains		12.7	27.3	9.7	8.3
Net gains on disposals of marketable securities		17.8	39.9	7.7	5.3
Financial expenses		**128.6**	**120.7**	**139.2**	**116.2**
Depreciation allowances & provisions		25.0	17.9	18.3	18.1
Interest and related expenses		88.3	76.6	106.0	89.3
Foreign exchange losses		13.4	24.3	13.8	7.7
Net losses on disposals of marketable securities		1.9	1.9	1.1	1.1
FINANCIAL INCOME (LOSS)	3	**489.7**	**513.2**	**394.7**	**102.6**
CURRENT PRE-TAX INCOME		**457.3**	**531.7**	**419.2**	**160.8**
Extraordinary income		**1,571.7**	**1,797.4**	**3,237.5**	**408.5**
On management transactions		8.1	6.0	4.9	4.7
On capital transactions		1,227.1	901.5	2,865.6	287.7
Reversals of provisions and expense transfers		336.5	890.0	367.0	116.2
Extraordinary expenses		**1,438.7**	**2,183.6**	**3,122.8**	**426.0**
On management transactions		16.9	27.2	12.6	11.8
On capital transactions		869.0	1,005.9	2,372.9	242.9
Depreciation allowances & provisions		552.8	1,150.5	737.3	171.3
EXTRAORDINARY INCOME	4	**132.9**	**(386.2)**	**114.6**	**(17.5)**
Employee profit-sharing		(5.4)	(5.3)	(3.1)	(2.3)
Corporate income tax	5	106.4	197.8	81.3	4.8
NET INCOME		**691.2**	**337.9**	**612.0**	**145.9**

BALANCE SHEET - ASSETS

In millions of EUR

	Note No.	1998 Gross	1998 Dep., Amort. & Prov.	1998 Net	1997 Net	1996 Net pro forma	1996 Net reported
Fixed assets							
Intangible assets	6	**607.5**	**185.3**	**422.2**	**440.0**	**454.2**	**453.7**
Tangible assets	6	**4,251.4**	**1,355.5**	**2,895.9**	**2,914.6**	**2,987.9**	**2,979.9**
Assets owned outright							
Land		24.3	0.6	23.7	23.7	25.6	21.0
Buildings		87.7	52.8	34.9	37.3	61.0	58.7
Machinery, equipment, tooling, fixtures & fittings		164.3	120.7	43.6	36.8	77.7	77.7
Other fixed assets		64.8	50.0	14.8	15.1	16.6	15.6
Assets under concession							
Assets placed under concession by the concession holder		697.1	227.5	469.6	483.3	444.9	444.9
Assets placed under concession by the concession grantor		3,135.8	903.9	2,231.8	2,234.9	2,255.9	2,255.9
Tangible assets in progress		**76.3**		**76.3**	**81.1**	**103.4**	**103.4**
Advances and down payments on assets		**1.2**		**1.2**	**2.4**	**2.8**	**2.8**
Long-term investments	7	**16,133.5**	**2,346.6**	**13,786.9**	**9,330.2**	**8,097.8**	**2,669.9**
Investments in subsidiaries and affiliates		15,565.9	2,286.9	13,279.0	8,208.7	7,343.5	2,585.0
Amounts due on investments		162.5	54.9	107.7	704.7	106.2	52.9
Other investment securities		345.0	4.5	340.4	336.6	314.0	28.5
Loans		58.5	0.3	58.2	78.8	332.7	2.2
Other long-term investments		1.7	0.0	1.7	1.5	1.4	1.3
TOTAL FIXED ASSETS		20,992.4	3,887.4	17,105.1	12,684.8	11,539.9	6,103.4
Current assets							
Inventories and work in progress		**94.6**	**0.9**	**93.8**	**88.4**	**87.1**	**87.1**
Advances and down payments to suppliers		**2.1**		**2.1**	**2.1**	**1.8**	**1.8**
Operating accounts receivable		**337.8**	**9.7**	**328.0**	**361.8**	**291.5**	**291.5**
Trade accounts receivable and related accounts		255.0	9.5	245.4	228.5	227.8	227.8
Other accounts receivable		82.8	0.2	82.6	133.2	63.6	63.6
Sundry receivables		**389.2**	**5.9**	**383.3**	**457.0**	**229.8**	**125.5**
Marketable securities	9	**339.8**	**9.0**	**330.8**	**372.9**	**1,294.6**	**424.7**
Cash and cash equivalents		**166.0**		**166.0**	**326.7**	**368.6**	**392.6**
TOTAL CURRENT ASSETS		1,329.5	25.5	1,304.0	1,608.8	2,273.3	1,323.1
Prepaid expenses	10	**95.5**		**95.5**	**114.0**	**130.1**	**130.1**
Unrealized foreign exchange losses		**2.0**		**2.0**	**1.9**	**0.9**	**0.8**
TOTAL ASSETS		22,419.4	3,912.8	18,506.6	14,409.5	13,944.3	7,557.4

BALANCE SHEET - LIABILITIES

In millions of EUR

	NOTE No.	1998	1997	1996 PRO FORMA	1996 REPORTED
Shareholders' equity					
Share capital		1,351.6	1,154.7		542.6
Additional paid-in capital		7,739.0	4,696.3		1,259.3
Revaluation adjustments	15	19.5	19.5		19.5
Reserves					
- Legal reserve		138.7	114.8		53.1
- Statutory reserves		931.5	923.4		72.5
- Other reserves		37.4	37.4		37.4
Retained earnings		4.7	44.8		22.1
Income for the year		691.2	337.9		145.9
Investment subsidies		3.8	10.3		9.1
Statutory provisions		15.9	17.5		18.2
TOTAL SHAREHOLDERS' EQUITY	11	10,933.2	7,356.5	7,059.6	2,179.4
Special concession accounts	12	**2,507.2**	**2,530.8**	**2,529.7**	**2,529.7**
Contingency and loss provisions	13	**2,104.8**	**1,766.0**	**1,086.1**	**583.9**
Liabilities					
Financial liabilities		**2,319.8**	**2,051.1**	**1,695.6**	**1,690.0**
Bond loans		1,050.1	1,077.6	1,291.9	1,291.9
Bank loans and borrowings		85.9	123.1	72.7	72.7
Sundry loans and long-term debt		85.3	67.9	61.3	58.3
Current accounts of subsidiaries		1,098.5	782.5	269.7	267.2
Advances and down payments received from customers		**18.8**	**10.5**	**7.2**	**7.2**
Operating liabilities		**355.2**	**373.4**	**308.9**	**303.8**
Trade notes and accounts payable		86.9	80.5	59.8	59.7
Other operating debts and borrowings		268.2	292.9	249.1	244.1
Sundry liabilities		**254.3**	**312.7**	**267.0**	**256.3**
Debt related to fixed assets and related accounts		204.0	220.5	239.3	238.8
Other debts		50.4	92.3	27.7	17.5
Total debts		**2,948.1**	**2,747.8**	**2,278.7**	**2,257.3**
Prepaid income		**8.8**	**6.4**	**989.7**	**6.5**
Unrealized foreign exchange gains		**4.4**	**2.0**	**0.6**	**0.6**
TOTAL LIABILITIES		18,506.6	14,409.5	13,944.3	7,557.4

INCOME STATEMENT

In millions of FRF

	NOTE NO.	1998	1997	1996 PRO FORMA	1996 REPORTED
Operating income		**8,660**	**8,525**	**7,959**	**7,941**
Revenues		7,759	7,629	7,306	7,306
Finished goods & in-progress inventory		32	5	89	89
In-house production		224	220	218	218
Operating subsidies		34	23	23	23
Reversals of provisions, amortization & depreciation and expense transfers		597	628	292	279
Other operating income		14	20	31	26
Operating expenses		**8,874**	**8,375**	**7,794**	**7,550**
Purchases of raw materials and other supplies		131	125	128	128
Changes in inventories		(4)	(2)	(2)	(2)
Other purchases and external charges		2,771	2,539	2,175	2,076
Management costs and fee payments		2,588	2,540	2,482	2,482
Taxes and related payments		190	184	185	157
Payroll expenses		1,927	1,903	1,833	1,751
Depreciation allowances & provisions		1,137	992	927	895
Fixed assets: depreciation allowances		574	564	545	525
Fixed assets: provisions		280	285	296	296
Current assets: provisions		43	30	28	28
Contingencies and losses: provisions		240	113	58	46
Other operating expenses		134	94	66	63
OPERATING INCOME (LOSS)	2	**(214)**	**150**	**165**	**391**
Share of income from joint operations		**0.2**	**(28)**	**(4)**	**(9)**

INCOME STATEMENT

In millions of FRF

	NOTE NO.	1998	1997	1996 PRO FORMA	1996 REPORTED
Financial income		**4,055**	**4,157**	**3,502**	**1,435**
Income from investments in subsidiaries and affiliates		3,444	3,384	2,958	1,070
Income from other marketable securities and non-current loans and advances		107	110	134	5
Other interest and related income		281	201	274	251
Reversals of provisions and expense transfers		23	22	21	21
Foreign exchange gains		83	179	64	54
Net gains on disposals of marketable securities		117	261	51	34
Financial expenses		**843**	**791**	**913**	**762**
Depreciation allowances & provisions		164	117	120	118
Interest and related expenses		579	502	696	586
Foreign exchange losses		88	159	90	51
Net losses on disposals of marketable securities		12	13	7	7
FINANCIAL INCOME (LOSS)	3	**3,212**	**3,366**	**2,589**	**673**
CURRENT PRE-TAX INCOME		**3,000**	**3,488**	**2,750**	**1,055**
Extraordinary income		**10,309**	**11,790**	**21,236**	**2,680**
On management transactions		53	39	32	31
On capital transactions		8,049	5,913	18,797	1,887
Reversals of provisions and expense transfers		2,207	5,838	2,407	762
Extraordinary expenses		**9,437**	**14,323**	**20,484**	**2,794**
On management transactions		111	178	83	77
On capital transactions		5,700	6,599	15,565	1,593
Depreciation allowances & provisions		3,626	7,546	4,836	1,124
EXTRAORDINARY INCOME	4	**872**	**(2,533)**	**752**	**(114)**
Employee profit-sharing		(36)	(35)	(20)	(15)
Corporate income tax	5	698	1,297	533	31
NET INCOME		**4,534**	**2,217**	**4,015**	**957**

BALANCE SHEET - ASSETS

In millions of FRF

	Note No.	1998 Gross	1998 Dep., Amort. & Prov.	1998 Net	1997 Net	1996 Net pro forma	1996 Net reported
Fixed assets							
Intangible assets	6	3,985	1,215	2,770	2,886	2,980	2,976
Tangible assets	6	27,888	8,890	18,998	19,119	19,599	19,547
Assets owned outright							
Land		159		159	160	168	138
Buildings		575	346	229	241	400	385
Machinery, equipment, tooling, fixtures & fittings		1,078	792	286	241	510	509
Other fixed assets		425	331	94	99	109	103
Assets under concession							
Assets placed under concession by the concession holder		4,573	1,492	3,081	3,170	2,918	2,918
Assets placed under concession by the concession grantor		20,569	5,929	14,640	14,660	14,798	14,798
Tangible assets in progress		501		501	532	678	678
Advances and down payments on assets		8		8	16	18	18
Long-term investments	7	105,828	15,393	90,435	61,202	53,118	17,513
Investments in subsidiaries and affiliates		102,105	15,001	87,104	53,845	48,170	16,956
Amounts due on investments		1,066	360	706	4,622	696	347
Other investment securities		2,263	30	2,233	2,208	2,060	187
Loans		383	2	381	517	2,183	15
Other long-term investments		11		11	10	9	8
TOTAL FIXED ASSETS		137,701	25,498	112,203	83,207	75,697	40,036
Current assets							
Inventories and work in progress		621	6	615	580	572	572
Advances and down payments to suppliers		14		14	14	12	12
Operating accounts receivable		2,215	64	2,151	2,373	1,911	1,911
Trade accounts receivable and related accounts		1,672	63	1,609	1,499	1,494	1,494
Other accounts receivable		543	1	542	874	417	417
Sundry receivables		2,552	39	2,513	2,997	1,507	824
Marketable securities	9	2,229	59	2,170	2,446	8,492	2,785
Cash and cash equivalents		1,088		1,088	2,143	2,418	2,575
TOTAL CURRENT ASSETS		8,719	168	8,551	10,553	14,912	8,679
Prepaid expenses	10	627		627	748	854	853
Unrealized foreign exchange losses		13		13	12	6	5
TOTAL ASSETS		147,060	25,666	121,394	94,520	91,469	49,573

BALANCE SHEET - LIABILITIES

In millions of FRF

	NOTE NO.	1998	1997	1996 PRO FORMA	1996 REPORTED
Shareholders' equity					
Share capital		8,866	7,574		3,559
Additional paid-in capital		50,765	30,806		8,260
Revaluation adjustments	15	128	128		128
Reserves					
- Legal reserve		910	753		348
- Statutory reserves		6,110	6,057		475
- Other reserves		245	245		245
Retained earnings		30	294		145
Income for the year		4,534	2,217		957
Investment subsidies		25	67		60
Statutory provisions		104	115		119
TOTAL SHAREHOLDERS' EQUITY	**11**	**71,717**	**48,256**	**46,308**	**14,296**
Special concession accounts	**12**	**16,446**	**16,601**	**16,594**	**16,594**
Contingency and loss provisions	**13**	**13,807**	**11,584**	**7,124**	**3,830**
Liabilities					
Financial liabilities		**15,217**	**13,454**	**11,122**	**11,086**
Bond loans		6,888	7,069	8,474	8,474
Bank loans and borrowings		563	807	477	477
Sundry loans and long-term debt		560	445	402	382
Current accounts of subsidiaries		7,206	5 133	1,769	1,753
Advances and down payments received from customers		**123**	**69**	**47**	**47**
Operating liabilities		**2,329**	**2,449**	**2,026**	**1,992**
Trade notes and accounts payable		570	528	392	391
Other operating debts and borrowings		1,759	1,921	1,634	1,601
Sundry liabilities		1,668	2,052	1,752	1,681
Debt related to fixed assets and related accounts		1,338	1,446	1,570	1,566
Other debts		330	606	182	115
Total debts		19,337	18,024	14,947	14,806
Prepaid income		58	42	6,492	43
Unrealized foreign exchange gains		29	13	4	4
TOTAL LIABILITIES		**121,394**	**94,520**	**91,469**	**49,573**

STATEMENT OF CHANGES IN CASH FLOW

In millions of EUR

	1998	1997	1996 PRO FORMA
Cash flow	602.9	527.3	624.3
Net increase in inventories and accounts receivable	174.4	(136.1)	(47.1)
Net increase in trade accounts payable	(23.2)	64.2	(48.9)
Accrued investment income	(1.7)	(28.4)	(32.6)
Interest expense and tax liabilities	(17.5)	(6.6)	7.6
CHANGES IN CASH FLOW FROM OPERATING ACTIVITIES	**734.9**	**420.4**	**503.3**
Purchases of tangible and intangible fixed assets	(88.7)	(105.6)	(121.3)
Disposals of tangible and intangible fixed assets	1.4	302.9	2.9
Purchases of securities and new loans granted	(5,867.3)	(1,655.9)	(1,587.8)
Disposals of securities and previous loans repaid	1,971.3	909.7	2,756.4
CHANGES IN CASH FLOW FROM INVESTMENT ACTIVITIES	**(3,983.3)**	**(548.9)**	**1,050.2**
New loans	100.0	58.2	4,455.8
Loan repayments	(186.9)	(254.7)	(4,774.1)
Increase in shareholders' equity	3,270.2	67.2	214.6
Dividends paid	(369.2)	(91.5)	(301.2)
CHANGES IN CASH FLOW FROM FINANCING ACTIVITIES	**2,814.1**	**(220.8)**	**(404.9)**
NET CHANGE IN CASH FLOW	**(434.3)**	**(349.3)**	**1,148.6**
Cash at beginning of period	134.6	483.9	(664.7)
Cash at year-end	(299.7)	134.6	483.9

STATEMENT OF CHANGES IN CASH FLOW

In millions of FRF

	1998	1997	1996 PRO FORMA
Cash flow	3,955	3,459	4,095
Net increase in inventories and accounts receivable	1,144	(893)	(309)
Net increase in trade accounts payable	(152)	421	(321)
Accrued investment income	(11)	(186)	(214)
Interest expense and tax liabilities	(115)	(43)	50
CHANGES IN CASH FLOW FROM OPERATING ACTIVITIES	**4,821**	**2,758**	**3,301**
Purchases of tangible and intangible fixed assets	(582)	(693)	(796)
Disposals of tangible and intangible fixed assets	9	1,987	19
Purchases of securities and new loans granted	(38,487)	(10,862)	(10,415)
Disposals of securities and previous loans repaid	12,931	5,967	18,081
CHANGES IN CASH FLOW FROM INVESTMENT ACTIVITIES	**(26,129)**	**(3,601)**	**6,889**
New loans	656	382	29,228
Loan repayments	(1,226)	(1,671)	(31,316)
Increase in shareholders' equity	21,451	441	1,408
Dividends paid	(2,422)	(600)	(1,976)
CHANGES IN CASH FLOW FROM FINANCING ACTIVITIES	**18,459**	**(1,448)**	**(2,656)**
NET CHANGE IN CASH FLOW	**(2,849)**	**(2,291)**	**7,534**
Cash at beginning of period	883	3,174	(4,360)
Cash at year-end	(1,966)	883	3,174

NOTE 1 - ACCOUNTING METHODS AND PRINCIPLES

The 1998 parent company accounts have been drawn up and presented in accordance with French generally accepted accounting principles and the valuation methods described hereafter, and they have been converted into euros using the official exchange rate (6.55957).

In order to give a true and fair view of the financial position of the company, two exceptions to the rules of presentation in the French General Chart of Accounts have been made in the income statement.

1 - In companies holding concessions, management of fixed assets under concession is a contractual obligation that is closely related to the public service function. Therefore, resulting disposals of fixed assets are recorded in operating income and not in extraordinary income. The same also applies to depreciation, amortization and provisions of any kind as well as various adjustments which may affect assets under concession. This exception to the rule, which makes it easier to assess operating income, does not affect fixed assets owned outright.

2 - In addition to its own activity as a company holding concessions in the public service field, the company manages a substantial portfolio of investments in subsidiaries and affiliates.

In order for financial income to remain representative of current income and to facilitate comparisons of fiscal years, all capital transactions relating to this portfolio are recorded as extraordinary income. These notably concern provisions and reversals of provisions for investments in subsidiaries and affiliates and amounts due on investments in subsidiaries and affiliates and, where applicable, losses on same (see Note 4 - Extraordinary income and Note 7 - Financial fixed assets).

For the sake of uniformity in presenting the income statement, these items are stated under extraordinary income and expenses, where gains and losses on disposals of investments in subsidiaries and affiliates are normally recorded.

Valuation methods

Intangible fixed assets:

Intangible fixed assets include:

- sums paid or payable constituting fees connected with the holding of concessions and amortized over the duration of the contract not yet elapsed; the portion of these commitments that is not yet due is stated in the debts related to fixed assets and related accounts;
- office software amortized over 12 months;
- other software, specific customizations and subsequent modifications resulting in its practical application in the technical, scientific and management sectors, amortized according to the straight-line method over a period of five years.

Tangible fixed assets:

Tangible fixed assets are valued at acquisition cost or at production cost with the exception of assets acquired before December 31, 1976 which were subject to statutory revaluation in 1976.

With the exception of land, tangible fixed assets are all depreciated according to the straight-line method. The main depreciation periods are as follows:

4-10 years	for tooling, vehicles, office and computer equipment,
5-20 years	for industrial equipment,
10 years	for furniture and fixtures and fittings,
15-40 years	for buildings and equipment relating to water collection and distribution.

Fixed assets placed under concession by the concession grantor:

Suez Lyonnaise des Eaux records under assets fixed assets which have an impact on added value. Fixed assets which the company is not contractually obliged to renew are thus not included. An equivalent value is recorded in the liabilities under "special concession accounts."

Long-term investments:

• Investments in subsidiaries and affiliates:

These represent long-term investments which make it possible to take control of the issuing company or to exercise significant influence over it or which make it possible to establish business relations with the issuing company.

If necessary, a loss provision is set aside in order to decrease the acquisition value to its usefulness value, determined with particular reference to equity value and financial return value.

In conjunction with the valuation of these securities, amounts due on them are, where applicable, depreciated where the risk is greater than the value of the securities.

Contingency provisions may be set aside if the company considers its commitment to be greater than the assets held or if there is a risk relating to certain investments which may not necessarily lead to a loss on assets.

- Other long-term investments:

These are investments held with a view to the long-term, but do not correspond to the criteria set out for investments in subsidiaries and affiliates.

Inventories and work in progress

Raw materials and consumables in inventories are booked at acquisition cost net of supplier discounts, rebates and reductions but excluding discounts for cash payments. This inventory is valued according to the average weighted cost method, which is calculated each time an addition is made to the inventory. A loss provision is set aside for items with slow turnover.

"Work in progress" includes:

- Work in progress, connected to our water distribution business,
- Estimated water supplies to our customers for which no meter-readings had been made at year-end. Such estimate is made at cost by customer sub-group.

Current asset receivables

These receivables are recorded in the balance sheet at nominal value and the risk of non-payment is analyzed on an individual basis. A provision is set aside to cover any risk of debtor insolvency for the amount of risk incurred.

In relation to amounts receivable from customers, a provision is set aside following the sending of a second request by registered mail. The customer's file is then sent to the litigation department.

Marketable securities

Depreciation of these securities, which consist mainly of listed securities, begins when their listed price is lower at year-end than their original cost.

Bond discounts

Bond loans, on which repayment is accompanied by discounts, are booked in the liabilities of the balance sheet at their total value, including said bond discounts. In return, these discounts are recorded in the assets and are amortized over the term of the loan in proportion to accrued interest.

Special concession accounts

These liabilities accounts comprise:

- The counterpart of fixed assets received free of charge from the concession grantor and recorded in the company's assets under "tangible fixed assets." Depreciation calculated on these assets has no impact on income and is charged to this liabilities account;
- Outside financing which may be provided to the concession holder for capital expenditures which he is obliged to make under the terms of the concession contract;
- Amortization of assets under concession, the purpose of which is to rebuild funds (after deduction of outside financing) invested by the concession holder in assets that must be returned free of charge to the concession grantor upon expiration of the contract. This amortization is deducted from income over the residual life of the contract.

Provision for renewal

Among the obligations borne by companies holding concessions is the obligation to renew water distribution and waste water installations which results in the company having to set aside the necessary provisions each year.

These provisions are calculated by estimating the replacement cost of the installations based on their usefulness value, applying a discount coefficient each year.

Insofar as the lifetime of fixed assets other than water pipes and mains is shorter than the life of the contract, the provision is calculated asset-by-asset, spreading their replacement value over the lifetime of the asset in question.

For water pipe systems, annual provisions are calculated contract-by-contract, with foreseeable partial replacement and renovation costs being spread over the life of each contract.

Transactions in foreign currencies

Foreign currency income and expenses are recorded at their equivalent value in French francs at the date of the transaction.

Amounts receivable and payable and cash in foreign currency are translated at year-end exchange rates. Translation differences are booked in the income statement for available cash and stated in the balance sheet under "unrealized foreign exchange gains and losses" for amounts receivable and payable. A provision is set aside for unrealized losses that are not covered.

Water sales

Water sales are recorded in accordance with an economic conception of revenues and include all amounts billed to customers, exclusive of value added tax, but including surtaxes and fees collected on behalf of third parties and management costs. A counterpart for these amounts received on behalf of local authorities is recorded under operating expenses under the item "management costs and other fee payments."

With respect to management contracts, the manager's remuneration is recorded in services provided.

Sales of water are booked when meter readings are made, which make it possible to determine amounts owed by customers.

If the water has not yet been supplied but a bill has been issued in accordance with the contract (pre-billed subscriptions), a provision, which is recorded in the liabilities on the balance sheet under loss provisions, is set aside at year-end for the expenses incurred as and when the water is supplied.

Revenues from the securities portfolio

Dividends are booked for their net amount in the fiscal year during which the decision to distribute them was made by the appropriate body.

Financial instruments

Suez Lyonnaise des Eaux is active in the derivatives markets.

Transactions not yet closed out at year-end are recorded as follows:

- Contracts on organized markets are marked to market;
- For over-the-counter (OTC) contracts, essentially interest rate swaps, the potential accrued interest differential is recorded.

Corresponding profits and losses are recorded as income in the same way as closed-out contracts.

Assets and liabilities in the balance sheet directly or indirectly affected by these financial instruments are valued at year-end in accordance with the relevant accounting principles.

Contracts not yet closed out are recorded in the off-balance sheet commitments at nominal value. They are set out in further detail in Note 17.6.

Corporate income tax

By an election on December 20, 1990 renewed on December 22, 1995, the company declared that, as from January 1, 1991, it was to become the parent company of a tax consolidation group within the meaning of the provisions of Articles 223 A *et seq.* of the French General Tax Code.

The tax consolidation agreement drawn up with the subsidiaries of the tax group applies the principle of tax neutrality: for each subsidiary involved, the tax charge to be recorded in its income statement and paid to Suez Lyonnaise des Eaux is calculated as if the company had been taxed separately.

Suez Lyonnaise des Eaux pays the French Treasury a tax corresponding to the tax income of the whole tax group, after offsetting profits and losses, in particular. This results in either a consolidation profit or loss, which is acquired by Suez Lyonnaise des Eaux and recorded in the results.

NOTE 2 - OPERATING INCOME (LOSS)

2.1 Breakdown of income by sector

In millions of EUR

	1998	1997
Water distribution	654.6	649.7
Waste water treatment	382.2	372.3
Works	41.6	41.6
Others	104.5	99.4
TOTAL	**1,182.9**	**1,163.0**
Of which exports	56.9	61.0

2.2 Other purchases and external charges

In millions of EUR

	1998	1997
Sub-contracting connected with the "works" sector	21.6	20.7
Purchases of supplies not inventoried	116.2	75.2
Outside personnel	23.1	20.3
Rental expenses	34.8	35.1
Fees and remuneration of intermediaries	83.4	88.4
Maintenance	48.3	47.3
Other external services	95.0	100.1
TOTAL	**422.4**	**387.1**

2.3 Payroll expenses

In millions of EUR

	1998	1997
Wages and salaries	187.6	187.7
Social security contributions	106.1	102.5
TOTAL	**293.7**	**290.2**

2.4 Assets under concession

The book value of assets under concession removed from the assets because they became obsolete during the fiscal year stands at EUR 16.78 million, for a retirement value of EUR 0.05 million.

2.5 Operating depreciation, amortization and provisions and reversals thereof

Operating depreciation, amortization and provisions and reversals thereof may be broken down as follows:

In millions of EUR

	Dep., amortiz., prov. 1998	Reversals 1998	Dep., amortiz., prov. 1997	Reversals 1997
Depreciation & amortization	**87.5**	**12.7**	**85.9**	**15.4**
Intangible assets	30.6		28.6	
Tangible assets	29.4	2.3	35.4	4.4
Assets under concession	26.4	10.4	20.9	11.0
Expenses to be accrued	1.1		1.0	
Provisions	**85.8**	**50.8**	**65.2**	**35.9**
Renewal	42.7	36.9	43.5	27.3
For current assets	6.5	4.9	4.6	3.0
For expenses	36.6	9.0	17.2	5.6
Expense transfers		**27.6**		**44.5**
TOTAL	**173.3**	**91.1**	**151.3**	**95.8**

NOTE 3 - FINANCIAL RESULTS

In millions of EUR

	1998	1997
Dividends on investments in subsidiaries and affiliates	520.0	509.0
Net income on investment transactions	16.5	53.4
Net expenses on financing transactions	(43.9)	(50.0)
Other income and expenses	(2.9)	0.8
TOTAL	**489.7**	**513.2**

NOTE 4 - EXTRAORDINARY INCOME

There was extraordinary income of EUR 132.9 million due to the following transactions:

- disposals, including: Saint Gobain (EUR 394.54 million), San Paolo di Torino (EUR 32.47 million), contributions of Electricité de Tahiti securities to Elyo (EUR 27.59 million).
- depreciation of foreign subsidiary securities (EUR 29.58 million) including EUR 17.68 million for Palyja (Indonesia);
- additional loss provisions for Crédisuez (EUR 289.35 million) and emerging countries (EUR 38.11 million);
- recovery of contingency provisions in the "facilities/construction" sector (EUR 79.88 million).

NOTE 5 - CORPORATE INCOME TAX

In millions of EUR

	1998
Tax on current income (including profit-sharing)	10.5
Tax on extraordinary income	(123.2)
Tax consolidation gain for the fiscal year	219.1
NET CORPORATE INCOME TAX	**106.4**

NOTE 6 - TANGIBLE AND INTANGIBLE ASSETS

6.1 Gross values

In millions of EUR

	1997	Changes during the fiscal year		1998
		Increases	Decreases	
Intangible assets	**596.5**	**19.2**	**8.2**	**607.5**
Tangible assets	**4,193.5**	**300.8**	**242.9**	**4,251.4**
Assets owned outright	329.9	23.0	11.9	341.0
Assets placed under concession by the concession holder	720.8	71.9	95.6	697.1
Assets placed under concession by the concession grantor	3,059.3	205.8	129.3	3,135.8
Tangible assets in-progress	81.1	0.1	4.9	76.3
Advances and down payments on fixed assets	2.4		1.2	1.2
TOTAL	**4,790.0**	**320.0**	**251.1**	**4,858.9**

6.2 Depreciation & amortization

In millions of EUR

	1997	Changes during the fiscal year		1998
		Increases	Decreases	
Intangible assets	**156.6**	**30.5**	**1.8**	**185.3**
Tangible assets	**1,278.8**	**172.4**	**95.7**	**1,355.5**
Assets owned outright	216.9	18.6	11.6	223.9
Assets placed under concession by the concession holder	237.5	26.9	36.8	227.6
Assets placed under concession by the concession grantor	824.4	126.9	47.3	904.0
TOTAL	**1,435.4**	**202.9**	**97.5**	**1,540.8**
including:				
With regard to operating income		59.9		
With regard to liability counterpart		142.8		

(depreciation of assets under concession - financing of third parties - fixed assets of the concession grantor)

NOTE 7 - FINANCIAL FIXED ASSETS

7.1 Gross values

In millions of EUR

	1997	Changes during the fiscal year		1998
		Increases	Decreases	
Investments in consolidated subsidiaries and affiliates	9,597.1	5,574.8	37.7	15,134.2
Investments in unconsolidated subsidiaries and affiliates	960.1	34.1	562.5	431.7
Amounts due on investments	760.6	26.3	624.4	162.5
Other long-term investments	341.3	866.0	862.3	345.0
Other financial fixed assets	82.3	9.4	31.6	60.1
Total	**11,741.4**	**6,510.6**	**2,118.5**	**16,133.5**

In relation to securities:

- the main acquisitions relate to Société Générale de Belgique (EUR 3,931.4 million), following the public offer of exchange, Crédisuez (EUR 897.2 million capital increase) and Sita (EUR 217.4 million capital increase) and Elyo (EUR 220 million capital increase in cash and contribution of Electricité de Tahiti)
- the divestments relate to disposals of Saint Gobain securities to Saint Gobain itself (EUR 457 million), of Stralex securities to our subsidiary Fided (EUR 35.8 million), of Hungarian Fovarosi Vismuvek securities to the project subsidiary Hungariaviz (EUR 38.6 million), to the contribution of Electricité de Tahiti to Elyo (EUR 47.1 million).

Amounts due on investments take into account the removal of an amount of EUR 609.8 million for Crédisuez that has been capitalized.

The other long-term investments represented buyback movements (EUR 793 million) and cancellation movements (EUR 729.8 million) for Suez Lyonnaise des Eaux securities; at year-end, this entry included 387,824 Suez Lyonnaise des Eaux securities (EUR 63.4 million), plus 79,232 securities entered as marketable securities allocated to the exercise of the stock options granted.

7.2 Provisions

In millions of EUR

	1997	Changes during the fiscal year		1998
		Increases	Decreases	
Investments in consolidated subsidiaries and affiliates	2,263.1	27.9	107.8	2,183.2
Investments in unconsolidated subsidiaries and affiliates	85.5	23.5	5.3	103.7
Amounts due on investments	55.8	0.6	1.5	54.9
Other long-term investments	4.7	1.2	1.4	4.5
Other financial fixed assets	2.1		1.8	0.3
Total	**2,411.2**	**53.2**	**117.8**	**2,346.6**

NOTE 8 - BREAKDOWN OF RECEIVABLES BY MATURITY DATE

In millions of EUR

	Gross value as of Dec. 31. 1998	Maximum of 1 year	1-5 years	Over 5 years
Fixed assets	**222.6**	**121.7**	**46.4**	**54.5**
Amounts due on investments	162.5	113.3	40.1	9.1
Loans	58.4	8.4	4.6	45.4
Other long-term investments	1.7		1.7	
Current assets	**733.5**	**705.5**	**27.5**	**0.5**
Trade notes and accounts receivable	255.0	229.0	25.5	0.5
Other receivables	471.8	469.8	2.0	
Prepaid expenses	6.7	6.7		
Total	**956.1**	**827.2**	**73.9**	**55.0**

NOTE 9 - MARKETABLE SECURITIES

The marketable securities in the balance sheet which amount to EUR 330.81 million had a market value of EUR 340.27 million as of December 31, 1998.

NOTE 10 - ACCRUAL ACCOUNTS

In millions of EUR

	1998	1997
Prepaid expenses	**95.5**	**114.0**
Prepaid expenses	6.7	6.7
Expenses to be accrued over several fiscal years	8.9	9.9
Bond discounts to be amortized	79.9	97.4
Prepaid income	**8.8**	**6.4**
Prepaid income	8.8	6.4

NOTE 11 - SHAREHOLDERS' EQUITY

11.1 Changes in shareholder's equity

In millions of EUR

Shareholders' equity at 1997 year-end (not including income)	**7,018.6**
Allocation of 1997 income to shareholders' equity	(31.4)
Shareholders' equity at beginning of 1998	**6,987.2**
Increase in capital following the public offer of exchange with regard to Société Générale de Belgique	3,908.3
Cancellation of treasury stock	(729.8)
Other changes in the 1998 fiscal year:	
- conversion of bonds	23.1
- subscription of shares reserved for employees	61.3
- changes in subsidies and statutory provisions	(8.1)
Shareholders' equity at 1998 year-end (not including income)	**10,242.0**

11.2 Breakdown of share capital

In millions of EUR

	NUMBER	PAR VALUE (1) (in EUR)	AMOUNT (in millions of EUR)
Shares making up share capital at beginning of fiscal year	**126,235,772**	**9.15**	**1,154.6**
Shares issued during the fiscal year:			
Increase in capital following the public offer of exchange with regard to Société Générale de Belgique	25,396,358	9.15	232.3
Cancellation of treasury stock	(4,759,580)	9.15	(43.6)
Conversion of bonds	217,101	9.15	2.0
Exercise of stock options by employees	417,421	9.15	3.8
Subscriptions to the investment fund reserved for employees	260,665	9.15	2.4
Shares making up share capital at year-end	**147,767,737**	**9.15**	**1,351.5**

(1) This par value is only the equivalent of the par value in FRF and does not correspond to the par value resulting from the official conversion of capital into euros as of 1999.

NOTE 12 - SPECIAL CONCESSION ACCOUNTS

In millions of EUR

	1998	1997
Fixed assets placed under concession by the concession grantor (2)	2,231.9	2,234.9
Fixed assets financed by third parties	64.3	96.3
Amortization of assets under concession	211.0	199.6
TOTAL	**2,507.2**	**2,530.8**

(2) Corresponds to the net book value of assets provided free of charge by the local authority when a contract is signed or an amendment is signed thereto and whicb Suez Lyonnaise des Eaux is under an obligation to renew.

NOTE 13 - STATUTORY PROVISIONS AND CONTINGENCY AND LOSS PROVISIONS

In millions of EUR

	1997	Changes during the fiscal year		1998
		Increases	Decreases	
Statutory provisions	**17.5**	**2.0**	**3.6**	**15.9**
Special revaluation provision	8.4	0.0	2.1	6.3
Others	9.1	2.0	1.5	9.6
Contingency and loss provisions	**1,766**	**577.7**	**238.9**	**2,104.8**
Sector-related risks	1,166.1	371.8	148.8	1,389.1
Risks relating to emerging countries	38.1	38.1	0.0	76.2
Pension liabilities	108.9	2.2	0.0	111.1
Renewal	352.9	42.7	64.0	331.6
Other contingencies and losses	100.0	122.9	26.1	196.8
TOTAL	**1,783.5**	**579.7**	**242.5**	**2,120.7**
Including provisions and reversals of provisions				
- Operating		79.3	45.9	
- Financial		2.0	2.6	
- Extraordinary		498.4	165.1	

The purpose of provisions for sector-related risks and risks relating to emerging countries is to hedge potential or existing risks connected with the business of our subsidiaries, particularly in the real estate field and in foreign countries. The EUR 111.1 million pension plan commitment provision covers firstly commitments made to former Lyonnaise des Eaux personnel for EUR 97.1 million (Note 18) and, secondly, commitments made to former Compagnie de Suez personnel which amount to EUR 14 million.

The renewal provision records, in particular, the impact of contracts ending.

Beyond the various contingencies and losses connected with our water distribution business, these provisions take into account the impact of a draft agreement on early retirement measures proposed to employees of the company.

NOTE 14 - BREAKDOWN OF DEBTS AND LIABILITIES BY MATURITY DATE

In millions of EUR

	GROSS VALUE AS OF DEC. 31, 1998	MAXIMUM OF 1 YEAR	1-5 YEARS	OVER 5 YEARS
Long-term debts	**2,319.8**	**1,632.3**	**647.1**	**40.4**
Convertible bond loans	1,050.1	420.1	630.0	
1990 6.50% convertible bonds	399.4	399.4		
1996 4% convertible bonds	650.7	20.7	630.0	
Bank loans and borrowings	85.8	85.8		
Miscellaneous loans and long-term debt	85.4	27.9	17.1	40.4
Current accounts of subsidiaries	1,098.5	1,098.5		
Trade payables and sundry liabilities	**618.3**	**475.0**	**86.1**	**57.2**
Trade notes and accounts payable	86.9	86.4	0.3	0.2
Tax and social security liabilities	88.7	88.3	0.5	
Other trade payables	179.5	179.4	0.2	
Debts related to fixed assets and related accounts	204.0	61.7	85.2	57.0
Other sundry liabilities	50.3	50.3		
Prepaid income	8.8	8.8		
TOTAL	**2,938.1**	**2,107.3**	**733.3**	**97.6**

NOTE 15 - REVALUATION

In millions of EUR

	1997	CHANGES DURING THE FISCAL YEAR ADDITIONAL DEPREC. & AMORT.	DECREASES DUE TO DISPOSALS	1998
Provisions				
Land	0.3		0.2	0.1
Buildings	1.5	0.2	0.2	1.1
Machinery, equipment and tooling	6.7	0.6	1.1	5.0
TOTAL PROVISIONS	**8.2**	**0.8**	**1.3**	**6.1**
Reserve				
Investments in subsidiaries and affiliates	19.5			19.5

NOTE 16 - ITEMS RELATING TO SUBSIDIARIES AND AFFILIATES WHICH COME UNDER SEVERAL BALANCE SHEET ENTRIES

In millions of EUR

	SUBSIDIARIES	AFFILIATES
Investments	12,521.1	349.9
Amounts due on investments	95.0	3.5
Trade notes and accounts receivable	6.3	
Other receivables (including debit balances in current accounts of subsidiaries)	217.8	8.4
Credit balances in current accounts of subsidiaries	999.2	
Trade notes and accounts payable	4.6	1.1
Other liabilities	5.9	15.2

NOTE 17 - FINANCIAL COMMITMENTS

17.1 Former Lyonnaise des Eaux pension commitments

The amount of commitments given with respect to vested pension commitments and retirement benefits corresponds, firstly, to all of the rights acquired as of December 31, 1988 by all current personnel or former employees who had retired at that date in respect of the previous pension plan, and, secondly, to contractual retirement indemnities and benefits, the amount of which is updated as of December 31 of each year.

These commitments are valued on the basis of the following actuarial assumptions:

- annual interest rate:	5.06%
- annual salary increase rate:	2%
- annual company pension plan increase rate:	2%
- mortality tables:	TV 88-90

The sum of commitments calculated in this way amounted to EUR 170.4 million as of December 31, 1998 and is broken down as follows:

- **Retirees**	**93.6**
. covered by insurance	66.0
. covered by a provision	27.6
- **Current personnel**	**76.8**
. covered by insurance	7.1
. covered by a provision	69.7

Starting from January 1, 1989, the date of implementation of the new contributory pension plan, commitments have been limited to the payment of fixed contributions to an insurance company.

17.2 Former Compagnie de Suez pension commitments

Commitments with respect to retirement benefits granted to employees by the former Compagnie de Suez can be broken down into four categories:

- pensions paid to Compagnie du canal de Suez retirees
- pensions paid to Banque de Suez retirees
- supplemental pensions paid to former employees in accordance with agreements entered into between 1988 and 1993.
- a guaranteed pension, for which the pension plan was closed in 1995 by Compagnie de Suez's board of directors, that shall be paid to a specified group of retirees.

In order to provide for these future expenses, a EUR 14 million provision has been booked on the balance sheet.

17.3 Leasing

Leased assets

In millions of EUR

	Original value	Lease payments for the fiscal year	Accumulated lease payments	Depreciation expense for the fiscal year	Accumulated depreciation
Buildings	60.8	3.4	13.3	1.4	3.8
Other tangible fixed assets	63.1	7.5	32.9	4.3	25.6
Total	**123.9**	**10.9**	**46.2**	**5.7**	**29.4**

Leasing commitments

In millions of EUR

	Lease payments remaining due				
	Less than 1 year	1-5 years	More than 5 years	Total	Residual purchase price
Buildings	3.5	13.4	39.2	56.1	0
Other tangible fixed assets	8.5	23.9	18.6	51.1	0.2
Total	**12.0**	**37.3**	**57.8**	**107.2**	**0.2**

17.4 Commitments given

In millions of EUR	
International contract guarantees	648.2
Real estate sector guarantees	288.0
Sale agreement guarantees	573.2
Guaranteed value certificate commitments	696.8
Others	133.2

The 25,396,358 guaranteed value certificates were issued at the time of the public offer of exchange with regard to Société Générale de Belgique and entitle holders to receive, between December 29, 2000 and March 30, 2001, a sum in French francs that is equal to the difference, if positive, between EUR 167.69 and the listed market price of Suez Lyonnaise des Eaux shares, as defined in the offer of exchange, up to EUR 27.44 per GVC.

The commitments given correspond to 25,396,358 outstanding GVCs for EUR 27.44 each. The market value of the GVCs as of December 31, 1998 amounted to EUR 154.89 million.

Other commitments were given to the authorities in Hong Kong, to guarantee the performance of agreements acquired by Sita from Browning-Ferries Industries; this guarantee is counter-guaranteed by our subsidiary Sita.

Suez Lyonnaise des Eaux made commitments by way of option agreements:

- to A.I.G. - "Asian Infrastructure Fund LP" and "Tropical Excellence Infrastructure Pte Ltd" to buy back the Lyonnaise Asia Water Limited shares subscribed by these two companies.
- to allow holders of Lyonnaise des Eaux equity warrants, which relate to Northumbrian shares, to transfer to Lyonnaise des Eaux the purchase of one Northumbrian Water Group PLC share for the price of GBP 1.96 provided that holders can prove that they has already acquired the 35 warrants required to apply for one Lyonnaise des Eaux share.

17.5 Commitments received

In millions of EUR	
Return to profit	142.7
Others	35.7

17.6 Reciprocal commitments

In millions of EUR	
Rate swaps	215.9
Forward exchange contracts	35.4
Options	815.3 *

* This line primarily concerns put and call options for shares and convertible bonds in AXA.

NOTE 18 - VALUATION OF DEFERRED TAXES AT YEAR-END

In millions of EUR

	Deferred tax: assets (liabilities)		
Type of timing differences	1997	Variations	1998
Non tax-deductible expenses or temporarily non-taxable income	534.9	95.8	630.7
Pension commitment provisions	39.8	0.9	40.7
Expenses deducted for tax purposes but not yet booked for accounting purposes	(9.9)	8.8	(1.1)
Income taxed but not yet booked for accounting purposes	7.5	(6.3)	1.2
Difference between value of securities for accounting and tax purposes	(9.3)	2.1	(7.2)
Total	**563.0**	**101.3**	**664.3**

NOTE 19 - AVERAGE WORKFORCE

	1998	1997
Company personnel	**5,494**	**5,503**
Senior management and executives	769	747
Lower management and supervisory staff	1,062	1,048
Workers, employees, technical staff	3,663	3,708
Personnel on loan to the company	**12**	**18**

NOTE 20 - PLAN FOR THE YEAR 2000 DATE CHANGE AND THE CHANGEOVER TO THE EURO

The company has prepared for these two deadlines by setting up a working group in June 1996 with the purpose of preparing the information systems for the year 2000 date change and the changeover to the euro.

The plan takes into account, not only management hardware and software, but also all the data processing and technical electronic equipment for the catchment, treatment, production and distribution of water and for waste water treatment to provide for the continuity of public service at the time of the year 2000 date change.

Any possible consequences for building management systems, including the impact on heating systems, elevators and control of access to the buildings themselves as well as the impact on automotive equipment, are also taken into account.

Furthermore, the Company is contacting its main suppliers and subcontractors in order to obtain an assurance that they have implemented the necessary means to ensure continuity of supplies and services. Measures will also be taken in order to avoid any disruption of supplies during this period.

Finally, contingency plans will be implemented in order to deal with any incidents that may arise despite the preparations so as to ensure continuity in the provision of water and waste water treatment services to the public.

A large portion of our internal IT resources and those of our subcontractors have been allocated to the crucial year 2000 project. Thus, the changeover to the euro for most of our management systems has been postponed to 2001. However, steps have been taken to provide billing and pay slip information in euros and to accept payments from our customers in euros as of January 1, 1999.

From a financial standpoint, the measures implemented occasionally coincide with the replacement of certain hardware or software that was already planned or with the changes required as a result of the changeover to the single currency. Thus, it can be difficult to establish the costs that only relate to the year 2000 issue.

Overall expenditure is estimated at approximately EUR 18.6 million: EUR 5.2 million have already been used and EUR 9.4 million have been booked in provisions, while EUR 4 million remains to be invested.

Five-year financial summary of the company

	1998	1997	1996	1995	1994
I) Capital at year-end					
Share capital (in EUR)	1,351,622,777.1	1,154,671,162.9	542,552,993.6	530,940,650.1	519,435,892.9
Number of existing ordinary shares	147,767,737	126,235,772	59,315,239	58,045,706	56,787,935
Maximum number of shares to be issued in the future					
. By bond conversion (1)	9,368,899	9,586,000	9,586 231	2,951,714	2,951,714
. By the exercise of subscription rights (2)	2,060,658	2,492,585	1,760,600	1,521,650	1,286,250
. By the exercise of Northumbrian stock purchase warrants (3)	976,513	976,513	1,998,203		
II) Operations and income for the fiscal year (in millions of EUR)					
Revenues before tax	1,803.3	1,799.8	1,336.7	1,239.6	1,188.5
Income before tax, employee profit-sharing, depreciation, amortization and provisions	937.7	520.6	319.4	345.9	271.7
Corporate income tax expense (gain)	(106.4)	(197.7)	(4.7)		2.3
Employee profit-sharing due for the fiscal year	5.5	5.3	2.3	2.0	3.4
Income after tax, employee profit-sharing, depreciation, amortization and provisions	691.2	338.0	145.9	123.3	120.4
Dividends distributed	527.0	369.2	118.1	101.8	123.2
III) Earnings per share (in EUR) (4)					
Income after tax and employee profit-sharing but before depreciation, amortization and provisions	7.0	5.6	5.3	5.9	4.7
Income after tax, employee profit-sharing, depreciation, amortization and provisions	4.7	2.7	2.5	2.1	2.1
Dividends allocated per share	2.7	2.3	1.8	1.8	1.8
IV) Personnel					
Average workforce employed during the fiscal year	5,494	5,503	5,358	5,229	5,110
Total payroll for the fiscal year (in millions of EUR)	187.7	187.7	170.7	165.3	158.2
Total amounts paid during the fiscal year in respect of social benefits (social security, contributions to welfare schemes and charitable works, etc.) (in millions of EUR)	106.1	102.6	96.2	93.1	86.9

(1) - following the issue:

- in 1990 of 2,953,740 bonds at the current rate of one bond per share (as of December 31, 1998: 2,810,358 bonds remaining, i.e. 2,810,358 shares)
- in 1996 of 6,634,616 bonds at the current rate of one bond per share (as of December 31, 1998: 6,558,541 bonds remaining, i.e. 6,558,541 shares)

(2) - stock options for the benefit of Group personnel

(3) - following the issue in 1996 by Northumbrian of 69,937,105 shares to each of which is attached one Suez Lyonnaise des Eaux equity warrant which entitles the holder to subscribe to one share for 35 warrants (as of December 31, 1998: 34,177,955 warrants, i.e. 976,513 shares)

(4) - based on 147,767,737 shares existing as of December 31, 1998.

GENERAL STATUTORY AUDITORS' REPORT

To the Shareholders of Suez Lyonnaise des Eaux,

In compliance with the assignment entrusted to us at the Annual General Meeting of Shareholders, we hereby present to you our report relating to the fiscal year ended December 31, 1998 on:

• the audit of the accompanying parent company accounts of Suez Lyonnaise des Eaux, drawn up in French francs,

• the specific verifications and information stipulated by the law.

These parent company accounts have been approved by the Executive Board. Our role is to express an opinion on these accounts based on our audit.

1. Opinion on the parent company accounts

We conducted our audit in accordance with the professional standards applied in France. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the accounts. An audit also includes assessing the accounting principles used and significant estimates made by management to draw up the accounts, as well as evaluating the overall accounts presentation. We believe that our audit provides a reasonable basis for our opinion as expressed hereafter.

In our opinion, the financial statements give a true and fair view of the Company's financial position, and its assets and liabilities as of December 31, 1998, and of the results of operations of the company for the year then ended.

2. Specific verifications and information

We also performed the verifications specifically stipulated by law, in accordance with the generally accepted auditing standards.

We have no comments to make as to the fair presentation and conformity with the parent company accounts of the information provided in the management report of the Executive Board and in the documents sent to the shareholders relating to the company's financial position and accounts.

In accordance with the law, we have ensured that the various information relating to acquisitions and controlling interests and the identity of the shareholders has been provided to you in the management report.

Paris and Neuilly, April 16, 1999

The Statutory Auditors

Mazars & Guérard:
Frédéric Allilaire

Allilaire.

Barbier Frinault & Autres
Arthur Andersen:
Christian Chochon

SPECIAL STATUTORY AUDITORS' REPORT ON REGULATED AGREEMENTS

Parent company accounts - Fiscal year ended December 31, 1998

To the Shareholders of Suez Lyonnaise des Eaux,

Acting in our capacity as the statutory auditors of your company, we hereby provide you with our report on the regulated agreements.

In accordance with Article 145 of the Law of July 24, 1966, we were informed of the agreements that were previously authorized by your Supervisory Board.

It is not our responsibility to examine whether any other agreements exist, but rather to disclose, based on the information given to us, the main features, terms and conditions of those that have been brought to our attention, without having to give an opinion on their interest for the company or their well-founded nature. In accordance with the terms of Article 117 of the Decree of March 23, 1967, it is your responsibility to assess the interest for the company in entering into these agreements with a view to their approval.

We conducted our audit in accordance with the professional standards applied in France. Those standards require that we perform due diligence reviews to verify that the information that was given to us is consistent with the source documents from which this information is taken.

1. With Sita

Member of the Executive Board: Mr. Philippe Brongniart

Members of the Supervisory Board involved: Messrs. René Coulomb, André Jarrosson and Claude Pierre-Brossolette

At its meetings on January 14, 1998 and April 14, 1998, your Supervisory Board authorized the counter-guarantee granted by Sita to Suez Lyonnaise des Eaux for the guarantees granted by Suez Lyonnaise des Eaux to the authorities of Hong Kong within the scope of Sita's acquisition of the international business of Browning-Ferries Industries.

The amount and duration of this commitment are not stated.

This acquisition will take place in two separate stages:

• in January 1999, Crédit Agricole will acquire 70% of the capital of Banque Sofinco according to the following terms and conditions:

- 18% under the conditions of the call option provided for in the agreements entered into between the partners in August 1993,
- 52% by direct acquisition.

• in January 2000, Suez Lyonnaise des Eaux will transfer the remainder of its Sofinco shares - i.e., 30% - to Crédit Agricole.

The price of the 82% acquired through means other than the call option was established on the basis of a valuation of Banque Sofinco at FRF 10.39 billion. The total amount of the transaction will be FRF 9.15 billion, based on the value as of June 30, 1998.

2. With Caisse Nationale de Crédit Agricole

Member of the Supervisory Board involved: Mr. Lucien Douroux

At its meeting on April 14, 1998, your Supervisory Board Authorized the sale of 100% of Banque Sofinco to Crédit Agricole.

3. With Crédisuez

Members of the Executive Board involved: Messrs. Gérard Mestrallet, François Jaclot and Philippe Brongniart

At its meeting on April 14, 1998, your Supervisory Board authorized the Executive Board to grant the joint surety of Suez Lyonnaise des Eaux to the purchaser of ISM SA for the payment of all the sums due by Crédisuez for the implementation of the guarantees granted within the framework of the sale, that is a seller's guarantee with regard to assets and liabilities for the portion limited to 25% of the selling price, i.e. FRF 265 million.

At its meeting on October 14, 1998, your Supervisory Board authorized the granting of a joint surety covering all of Crédisuez's commitments within the scope of the sale of Banque La Hénin. These are seller's guarantees limited to 25% of the price of the transaction that are valid until the end of 2001, except for unlimited tax- and social security-type guarantees that are valid until the legal limitation period expires.

4. With Compagnie de Saint Gobain

Member of the Executive Board involved: Mr. Gérard Mestrallet

Member of the Supervisory Board involved: Mr. Pierre Faure

At its meeting on May 5, 1998, your Supervisory Board authorized the agreement planned between Suez Lyonnaise des Eaux and Compagnie de Saint Gobain to release their cross-shareholdings.

The planned agreement includes the following terms and conditions:

- following the adoption by the French Parliament of the law authorizing the acquisition of shares, Suez Lyonnaise des Eaux would buy 4.2 million Suez Lyonnaise des Eaux shares from Saint-Gobain while, for its part, Saint-Gobain would acquire 2.3 million Saint-Gobain shares,
- the prices applied for the exchange and sale were calculated, 1997 dividend off, on the basis of the average weighted prices of the last ten Stock Exchange trading sessions, which gave FRF 1,010.7 per Suez Lyonnaise des Eaux share and FRF 981.6 per Saint-Gobain share,
- the exchange would be performed by the two parent companies; unless the Law of December 31, 1998 were to come into effect, a substitution mechanism would enable Suez Lyonnaise des Eaux to acquire the shares held by Saint-Gobain, via a company within its Group.
- the 2.3 million Saint-Gobain shares still held by Suez Lyonnaise des Eaux following the exchange would be reclassified in co-operation with Saint-Gobain, either directly or by way of a bought deal.

5. With Degrémont and Northumbrian Water Group

Member of the Executive Board involved: Mr. Philippe Brongniart

Member of the Supervisory Board involved: Sir Frederick Holliday

At its meeting on October 14, 1998, your Supervisory Board authorized the guarantee and counter-guarantee to be granted within the scope of the joint offer made by Northumbrian Water Group and Degrémont for an agreement for the operation of a waste water treatment plant.

6. With Elyo

Members of the Executive Board involved: Messrs. Philippe Brongniart and François Jaclot

At its meeting on October 14, 1998, your Supervisory Board authorized the principle of a contribution to Elyo of the shares of Electricité de Tahiti that Suez Lyonnaise des Eaux held.

Within the context of the policy of re-centering and simplifying the Group's structures, it was contemplated that Suez Lyonnaise des Eaux would acquire the 29% of the capital of Electricité de Tahiti held by its subsidiary SPSP for the sum of FRF 206.6 million and then transfer its entire stake, which would thus have been increased from 39.8% to 68.8%, to Elyo in the form of a contribution in kind. The values envisaged would be FRF 1,031.25 per Electricité de Tahiti share and FRF 375 per Elyo share, which gives an exchange parity of 11 Elyo shares for 4 Electricité de Tahiti shares.

Furthermore, in accordance with the Decree of March 23, 1967, we were informed that the performance of the following agreements, approved during previous fiscal years, continued during the last fiscal year.

7. With Compagnie de Saint Gobain

The principle of a reduction in the cross-shareholding between your company and Compagnie de Saint Gobain was authorized in 1997, pursuant to which each company committed to halve its interest in the capital of the other over a period of twelve months following the request which would be made by the latter company. Furthermore, this board of directors' meeting authorized the granting of a mutual right of first refusal in relation to shareholdings until they have each fallen to less than 2% of the voting rights.

The complete release of the cross-shareholdings took place during the 1998 fiscal year.

8. With Degrémont

The return to profit clause, which was laid down at the time of the granting of subsidies to Degrémont in 1984, 1985 and 1987, was amended; through this amendment, Degrémont pledges to pay back the balance of the subsidies and cancellations of debt that were granted to it by Suez Lyonnaise des Eaux at a rate of 10% of its net book income over ten fiscal years as from 1991 up to the amount of sums due.

The repayment for 1998 provided for under this agreement stands at FRF 4 million.

9. With Dumez

In 1998, no repayments relating to the return to profit clause agreed to at the time of the cancellation of debt, which was granted by Suez Lyonnaise des Eaux to Dumez in 1992, were made.

10. With Elyo

The performance guarantee given by Suez Lyonnaise des Eaux to Elyo relating to the construction and running of a refuse incinerating plant in Rilieux-la-Pape is still effective.

11. With Sita

The guarantee granted by Suez Lyonnaise des Eaux relating to the Nent dump call for tenders is still effective.

12. With Eurawasser

The commitment given by Suez Lyonnaise des Eaux relating to the funding of investments to be made within the context of the water distribution and waste water treatment services contract for the city of Rostock (Germany) is still effective.

13. With Lyonnaise Europe

The purpose of this agreement is to guarantee GBP 13,015 million worth of loan notes issued by Lyonnaise Europe.

14. With Lyonnaise Deutchland

The agreement, which transformed the balance of the debt due by Lyonnaise Deutschland (i.e. DEM 45 million as of December 31, 1998) as well as the interest due and future interest payable into a subordinate debt whose repayment by Lyonnaise Deutschland would be subject to a return to profit or the recording of a liquidating dividend, is still effective.

15. With Compagnie Foncière Internationale (CFI)

In the context of commitments made by CFI to its employees in July 1994 and guaranteed by Compagnie de Suez, only two guarantees remain in force:

- supplementary redundancy indemnities for former CFI employees made redundant on December 31, 1999 at the latest,
- retirement indemnities relating to CFI employees transferred to Unibail (until September 30, 2004).

This agreement did not affect the 1998 fiscal year.

16. With Crédisuez and its direct and indirect subsidiaries

Following the decisions taken concerning the centralization of all of the real estate activities of the Compagnie de Suez group within the Crédisuez group, guarantees of value were granted by Compagnie de Suez and taken over by Suez Lyonnaise des Eaux at the time of the merger:

Guarantee granted to Réaumur participations and to three of its subsidiaries, Savipar, Financière Astorg Saussaies and SNC Partiel. The effects of this guarantee on the 1998 fiscal year were as follows:

- Suez Lyonnaise des Eaux was called upon for guarantees for a total amount of FRF 198 million;
- the total residual amount guaranteed was FRF 213 million as of December 31, 1998 for which full provisions were set aside in the accounts closed on that date;
- Compagnie de Suez made funds corresponding to the guarantees which had not been called at this date available in advance as from July 1, 1996. Funds transferred in this way do not bear interest.

Guarantee granted to Astofoncier. The effects of the guarantees granted at the time of the sales of Zeus and Sanrive on the 1998 fiscal year were as follows:

- Suez Lyonnaise des Eaux was called upon for guarantees for a total amount of FRF 85 million;
- the total residual amount guaranteed was FRF 118 million as of December 31, 1997 for which total amount provisions were set aside in the accounts closed on that date;

Compagnie de Suez granted three banking institutions first demand guarantees concerning three loans subscribed by Crédisuez for a total aggregate amount of FRF 1,600 million. These guarantees do not bear interest.

Compagnie de Suez authorized the granting of a 10-year joint surety to the group taking over Crédit à l'Habitation; this surety is limited to the guarantee relating to obligations, events or potential risks which might have affected the management of business debts contributed by Banque La Hénin and Banque Monod to the company sold and which were, for the most part, paid off.

17. With Suez Industrie

The counter-guarantee agreement signed in December 1995 by Compagnie de Suez for the benefit of Suez Industrie relating to a sum of FRF 165 million is still effective.
This counter-guarantee does not bear interest.
This agreement did not have any effect on the 1998 fiscal year.

18. With Bank Indosuez

• Operations resulting from the absorption of Compagnie La Hénin by Compagnie de Suez in 1991.
Suez Lyonnaise des Eaux previously guaranteed Banque Indosuez for FRF 337.15 million in repaying a bridging loan granted to Zeus. This guarantee ended in 1998, after Crédit Agricole Indosuez pulled out of the Zeus banking pool.
• Other operations
Compagnie de Suez took over all of Banque Indosuez's risk on an investment credit relating to two parts of the Réamur package in order to release it from such risk on a definitive basis. Following the sale of the parts of the Réamur package, Crédit Agricole Indosuez was reimbursed for FRF 210.6 million, and Foncière de l'Arcade was reimbursed for FRF 34.4 million. The guarantee was therefore closed out at year-end.

19. With Caisse Nationale de Crédit Agricole

Compagnie de Suez granted a seller's guarantee to Caisse Nationale de Crédit Agricole within the framework of the sale of the majority shareholding in Banque Indosuez to Caisse Nationale de Crédit Agricole. In 1998, no payments were made relating to this guarantee, which is limited to 24% of the selling price.

20. With Banque La Hénin

The authorization for Suez Lyonnaise des Eaux to sell shares that it held in the capital of Banque Monod to Banque La Hénin for the nominal sum of FRF 1 was accompanied by:

- a seller's guarantee limited to one year as from January 1, 1998 (except for tax guarantees which shall expire after January 1, 2000) and to a sum of FRF 50 million. This guarantee was called during the fiscal year in the amount of FRF 47 million.
- a guarantee on the value of the buildings held by Banque Monod in order to compensate for the loss which would result from the sale of these buildings. This guarantee applied only to requests made before December 31, 1997. The call under the guarantee was made before 1997 year-end in the amount of FRF 79,748 million.

Paris and Neuilly, April 16, 1999

The Statutory Auditors

Barbier Frinault & Autres:
Arthur Andersen
Christian Chochon

Mazars & Guérard:
Frédéric Allilaire

Allilaire.

LEGAL AND ADMINISTRATIVE INFORMATION

Information required by French law and administrative information

INFORMATION ABOUT THE COMPANY

Name (article 2 of the by-laws)

Suez Lyonnaise des Eaux.

Registered office (Article 5 of the by-laws)

72 avenue de la Liberté - 92000 Nanterre - France.
Administrative headquarters: 1 rue d'Astorg - 75008 Paris - France.

Legal form of the company (Article 1 of the by-laws)

French *Société Anonyme* (joint-stock corporation) with a Executive Board and Supervisory board governed by the Law of July 24, 1966, the Decree of March 23, 1967 and subsequent laws relating to business corporations.

Life (Article 4 of the by-laws)

Except in the event of early winding-up or extension, as provided for by law and the company's by-laws, the life of the Company shall end on December 31, 2040.

Corporate purpose (Article 3 of the by-laws)

The corporate purpose of the Company is to use all means to manage and promote its present and future assets in all countries, and in particular:

a) obtaining, purchasing, leasing and operating any concession or business relating to the supply of drinking or industrial water to cities, the removal and treatment of waste water, drainage and waste water services operations, irrigation and the construction of any installation used to transport, protect or store water.

b) obtaining, purchasing, leasing and operating all kinds of sales and services to municipalities and private individuals in connection with urban development and management of the environment.

c) studying, preparing and performing all public and private projects and works on behalf of municipalities and private individuals, drafting and conclusion of all agreements or contracts relating to the performance of such projects and works.

d) acquiring shares and ownership interests in existing or future companies, by means of subscription, purchase, contribution, exchange or by all other means, equity securities, shares, bonds, and any other security issued.

e) obtaining, purchasing, selling, licensing and utilizing all patents, patent licenses and processes.

f) in general, entering into all industrial, commercial, financial and property (personal or real property) transactions directly or indirectly related to the company's corporate purpose or likely to facilitate and promote the company's business.

The corporate purpose of the Company may, furthermore, be amended by the general meeting of shareholders in accordance with the law and Article 35 of its by-laws.

Company registration

The Company is registered in Nanterre under number B 542 062 559 02239. Its APE code is 410Z.

Consultation of legal documents relating to the Company

The legal documents relating to Suez Lyonnaise des Eaux may be consulted at the administrative headquarters of the Company: 1, rue d'Astorg - 75008 Paris - France.

Fiscal year (Article 37 of the by-laws)

The fiscal year of Suez Lyonnaise des Eaux begins on January 1 and ends on December 31 of each year.

Statutory appropriation of earnings (Article 39 of the by-laws)

One-twentieth of the profit generated, after deduction of any prior losses carried forward, is transferred to the legal reserve. This transfer ceases to be mandatory once the legal reserve reaches one-tenth of the share capital.

Any remaining profits (including any retained earnings) are available for distribution as dividends.

The following amounts are drawn on such distributable profits:

1) The amount needed to pay shareholders an initial dividend equivalent to 5% of the paid-in, unredeemed value of the share capital, without shareholders having any entitlement to claim payment of this dividend from profits generated in subsequent years, should the current year's earnings be insufficient to cover such an amount.
2) amounts that the Annual General Meeting of Shareholders has decided, on the Executive Board's recommendation, to carry forward or to transfer to reserves or a contingency fund set up for the purpose of total or partial redemption of the Company's shares, in particular.

Any remaining distributable profits are to be shared equally among the shareholders in proportion to the par value of their holdings, as a supplementary dividend.

Annual General Shareholders' Meetings

• Convening of meetings, conditions relating to attendance and the exercise of voting rights (Articles 26-34 of the by-laws)

All shareholders are entitled to attend the Annual General Shareholders' Meetings, regardless of the number of shares that they own.

A shareholder may only be represented by another shareholder or his/her spouse.

Each shareholder is entitled to as many votes as the number of shares that he/she owns or represents, without limitation, subject to the provisions of Articles 356-1, 356-4 and 359-1 of the Law of July 24, 1966. Dual voting rights are granted to holders of fully-paid in shares that have been registered in the shareholder's name for at least two years. Dual voting rights are also conferred immediately on any registered shares distributed without payment to a shareholder in respect of shares that already entitled the shareholder to such rights.

Dual voting rights are surrendered when registered shares are converted into bearer shares or when they change hands. However, a change of ownership through inheritance, the liquidation of marital community property between spouses or a donation *inter vivos* in favor of a spouse or a close relative does not result in the loss of such rights and also does not affect the calculation of the time limit after which such rights are acquired.

Shareholders present at meetings or their duly accredited proxies vote by show of hands, unless a secret ballot is requested either by the President or by shareholders jointly holding at least one-tenth of the share capital.

Any shareholder may vote by mail in accordance with the laws and regulations in force.

Voting forms that do not indicate the shareholder's intention or by which the shareholder abstains are counted as votes against the resolution in question.

A shareholder providing or enjoying a special benefit is not entitled to vote on a motion to approve that benefit on his own behalf or as a proxy, and his/her shares are not taken into account when calculating the majority vote and quorum.

• Compliance with ownership thresholds (Article 13 of the by-laws)

In addition to complying with the obligations contained in Articles 356-1 to 356-1-4 of the Law of July 24, 1966, any legal entity or individual who directly or indirectly owns a number of shares exceeding 1% of the share capital is required to inform the Company within fifteen days. This obligation also applies to each additional 1% of the share capital acquired.

Failure to comply with this obligation is penalized, at the request of one or more shareholders holding at least 5% of the share capital, by cancellation of the voting rights pertaining to the shares whose percentage ownership should have been declared. This cancellation applies to all shareholders' meetings held within two years as from the date on which the notification is duly effected.

• Identity of shareholders (Article 11 of the by-laws)

The Company may, at any time and in accordance with the laws and regulations in force, request the stock market clearing house to inform it of the identity or, in the case of a legal entity, the name, nationality and address of holders of shares conferring the immediate or future right to vote at its shareholders' meetings as well as of their individual ownership interests and any restrictions applicable to the shares.

INFORMATION ABOUT THE CAPITAL

Conditions laid down in the by-laws for changes in the capital and shareholders' rights

Any change in the capital or the rights conferred by shares must be made in accordance with Chapter II of the by-laws. The issue of new shares to increase capital can be approved only by the Extraordinary General Meeting, to which the Executive Board must submit a report on the proposed share issue.

If new shares are issued following capitalization of reserves, profits or premiums, the general meeting of shareholders shall vote subject to the quorum and majority requirements applicable to ordinary meetings of shareholders.

Amount of paid-in capital, number and classes of shares

As of December 31, 1998, the company's share capital had been fully subscribed and amounted to FRF 8,866,064,220, comprising 147,767,737 shares of a par value of FRF 60 each, all of the same class.

Significant transactions affecting the capital in 1998 were as follows:

- issue of 25,396,358 shares and GVCs, in July and August 1998, following the public offer of exchange with regard to Société Générale de Belgique,
- cancellation of 4,759,580 shares, on October 30, 1998, within the framework of a reduction in capital,
- subscription of shares by employees of the Company and related companies or economic interest groupings, under the terms of a company savings plan (resulting in the issue of 260,665 shares),
- exercise of employee stock options (resulting in the issue of 417,421 shares),
- conversion of June 1990 6.50% convertible bonds and January-February 1996 4% convertible bonds (resulting in the issue of 271,101 shares).

Converting the share capital into euros

On the basis of the authority given to it by the Ordinary and Extraordinary General Meeting of Shareholders on June 11, 1998 (13^{th} and 16^{th} resolutions), the Executive Board decided at its meeting on January 25, 1999, to convert the share capital into euros, rounding the par value of shares up to the nearest euro, thereby raising the par value from FRF 60 (equivalent to EUR 9.14694) to EUR 10 per share.

As of February 1, 1999, the share capital of Suez Lyonnaise des Eaux stands at EUR 1,477,677,370. It is divided into 147,767,737 shares with a par value of EUR 10 each, all of the same class.

CHANGES IN THE CAPITAL OF COMPAGNIE DE SUEZ OVER THE LAST 5 YEARS

YEAR	INCREASE IN CAPITAL	SHARE ISSUE PAR-VALUE (IN FRF)	ADDITIONAL PAID-IN CAPITAL (IN FRF)	CAPITAL (IN FRF)	NUMBER OF SHARES OUTSTANDING
DEC. 31, 1993				**11,556,069**	**154,080,921**
1994	- Issue of 22,859 shares with a par value of FRF 75 each through exercise of stock options	1,714	3,801	11,557,784	154,103,780
	- Issue of 1,091,878 shares with a par value of FRF 75 each through payment of a stock dividend	81,891	216,192	11,639,674	155,195,658
	- Issue of 6,161 shares with a par value of FRF 75 each through exercise of stock options	462	825	11,640,136	155,201,819
	- Issue of 243,539 shares with a par value of FRF 75 each through an increase in capital reserved for Group personnel	18,265	31,173	11,658,402	155,445,358
1995	- Issue of 3,228 shares with a par value of FRF 75 each through the exercise of stock options	242	439	11,658,644	155,448,586
	- Issue of 4,005,369 shares with a par value of FRF 75 each through the payment of a stock dividend	300,403	624,838	11,959,047	159,453,955
	- Issue of 400 shares with a par value of FRF 75 each through exercise of stock options	30	54	11,959,077	159,454,355
	- Issue of 128,267 shares with a par value of FRF 75 each through an increase in capital reserved for Group personnel	9,620	10,646	11,968,697	159,582,622
1996	- Issue of 4,064,162 shares with a par value of FRF 75 each through payment of a stock dividend	304,812	402,352	12,273,508	163,646,784
	- Issue of 116,598 shares with a par value of FRF 75 each through an increase in capital reserved for Group personnel	8,745	10,144	12,282,254	163,763,382
DEC. 31, 1996				**12,282,254**	**163,763,382**
JUNE 19, 1997				**12,282,254**	**163,763,382**

CHANGES IN THE CAPITAL OF LYONNAISE DES EAUX OVER 5 YEARS

DATE	TYPE OF TRANSACTIONS	PAR VALUE PER SHARE (IN FRF)	CAPITAL (IN FRF) (1)	ADDITIONAL PAID-IN CAPITAL(*) (IN FRF) (2)	NUMBER OF SHARES OUTSTANDING(3)
DEC. 31, 1993			**2,235,610,000**		**53,926,835**
June 9, 1994	exercise of March 1989 7.60% warrants exercise of stock options conversion of June 1990 6.50% bonds	60	141,972,060	772,579,512	2,366,201
Sept. 2, 1994	exercise of stock options conversion of June 1990 6.50% bonds payment of 1993 dividend (FRF 517) in stock	60	23,364,480	154,709,791	389,408
Jan. 18, 1995	exercise of stock options conversion of June 1990 6.50% bonds employee stock ownership plan	60	6,329,460	37,432,503	105,491
Sept. 27, 1995	payment of 1994 dividend (FRF 456) in stock exercise of stock options employee stock ownership plan	60	67,921,860	429,484,219	1,132,031
Jan. 10, 1996	exercise of stock options	60	7,544,400	48,247,100	125,740
Sept. 25, 1996	payment of 1995 dividend (FRF 451) in stock exercise of stock options conversion of January-February 1996 4% bonds	60	66,296,880	431,779,881	1,104,948
Jan. 15, 1997	employee stock ownership plan exercise of stock options conversion of January-February 1996 4% bonds	60	9,875,100	52,204,961	164,585
DEC. 31, 1996		**60**	**3,558,914,340**		**59,315,239**
	conversion of January-February 1996 4% bonds conversion of June 1990 6.50% bonds exercise of stock options	60	18,001,920	119,083,395	300,032
JUNE 19, 1997			**3,576,916,260**		**59,615,271**

(*) Additional paid-in capital: the amounts in this item correspond to changes in premiums on issues, contributions or mergers relating to capital transactions. They do not include amounts drawn on additional paid-in capital to cover expenses, transfers to the special long-term capital gains reserve, transfers to the legal reserve and a provision for retirement benefits.

CHANGES IN THE CAPITAL OF SUEZ LYONNAISE DES EAUX BETWEEN JUNE 19, 1997 AND DECEMBER 31, 1998

YEAR	INCREASE IN CAPITAL	SHARE ISSUE PAR-VALUE (IN FRF)	SHARE ISSUE ADDITIONAL PAID-IN CAPITAL (IN FRF)	CAPITAL (IN FRF)	NUMBER OF SHARES OUTSTANDING
JUNE 19, 1997 MERGER				**7,532,518,320**	**125,541,972***
	* *not taking into account the 300,032 Lyonnaise des Eaux shares issued during the first half of 1997 and recorded on January 5, 1998 by the Executive Board of Suez Lyonnaise des Eaux*			7,550,520,240	125,842,004
	- Issue of 272,539 shares with a par value of FRF 60 each through an increase in capital reserved for Group personnel	16,352,340	125,913,018	7,566,872,580	126,114,543
	- Issue of 121,105 shares with a par value of FRF 60 each through exercise of stock options	7,266,300	44,277,038	7,574,138,880	126,235,648
	- Issue of 3 shares with a par value of FRF 60 each through the conversion of June 1990 6.50% convertible bonds	180	2,220	7,574,139,060	126,235,651
	- Issue of 121 shares with a par value of FRF 60 each through the conversion of January-February 1996 4% convertible bonds	7,260	55,660	7,574,146,320	126,235,772
DECEMBER 31, 1997				**7,574,146,320**	**126,235,772**
	- Issue of 24,072,058 shares with a par value of FRF 60 each following the public offer of exchange (early July 1998) with regard to SGB	1,444,323,480	22,964,743,332	9,018,469,800	150,307,830
	- Issue of 1,324,300 shares with a par value 79,458,000 of FRF 60 each following the additional public offer of exchange (early August 1998) with regard to SGB	1,263,382,200	9,097,927,800	151,632,130	
	- Cancellation of 4,759,580 shares with a par value of FRF 60 each	-	-	8,812,353,000	146,872,550
	- Issue of 260,665 shares with a par value of FRF 60 each through an increase in capital reserved for Group personnel	15,639,900	192,370,770	8,827,992,900	147,133,215
	- Issue of 417,421 shares with a par value of FRF 60 each through exercise of stock options	25,045,260	168,926,910.81	8,853,038,160	147,550,636
	- Issue of 141,342 shares with a par value of FRF 60 each through the conversion of June 1990 6.50% convertible bonds	8,480,520	104,593,080	8,861,518,680	147,691,978
	- Issue of 75,759 shares with a par value of FRF 60 each through the conversion of January-February 1996 4% convertible bonds	4,545,540	34,849,140	8,866,064,220	147,767,737
DECEMBER 31, 1998				**8,866,064,220**	**147,767,737**
FEBRUARY 1, 1999	- Legal conversion of share capital into euros by capitalization of the sum of FRF 826,863,926 drawn from the item "additional paid-in capital" and correlative increase of the par value of shares from FRF 60 (equivalent to EUR 9.14694) to EUR 10.			1,477,677,370	147,767,737

Authorization to increase the capital

Authorization given by the General Meeting of Shareholders on June 11, 1998

Ordinary General Meeting of Shareholders

RESOLUTION	PURPOSE OF THE RESOLUTION	VALIDITY	MAXIMUM AMOUNT	AMOUNT USED
9th	Authority to trade in its shares on the Stock Exchange	1 year	Maximum purchase price: FRF 1,200 Minimum selling price: FRF 750 Maximum holding: 10%	4.1%
10th	Issue of bonds and debt securities	5 years	FRF 10 billion	FRF 4.6 billion in GVCs for the SGB public offer of exchange + EUR 787 million (FRF 5.2 billion) for the zero coupon bond loan with exchange options for AXA shares
	Bonds to result from the exercise of warrants	+	FRF 5 billion	

Extraordinary General Meeting of Shareholders

RESOLUTION	PURPOSE OF THE RESOLUTION	VALIDITY	MAXIMUM AMOUNT	AMOUNT USED
13th	Increasing the share capital, either by the issue, with maintenance of preferential subscription rights, of shares, warrants and/or marketable securities which give access to Company shares or by the capitalization of premiums*, reserves, profits or suchlike	26 months	FRF 4.5 billion (for the shares) FRF 5 billion (for the marketable securities)	None
14th	Increasing the share capital, by the issue, with elimination of preferential subscription rights, of shares, warrants and/or marketable securities which give access to company shares	26 months	FRF 4.5 billion (for the shares) FRF 5 billion (for the marketable securities)	FRF 1.52 billion for the SGB public offer of exchange
15th	Increasing capital at the time of a takeover bid or public offer of exchange	1 year	same as 14th	None
18th	Canceling shares	1 year	10% of the capital	4.8 million shares i.e. 3.2% of the capital**
19th	Granting stock subscription or purchase options	5 years	2% of the capital	1,041,000 shares i.e. 0.7% of the capital
20th	Increasing capital reserved for Group personnel	5 years	5% of the capital	260,665 shares i.e. 0.2% of the capital
21st	Authority to carry out convertible bond restructuring	1 year	the two types of existing convertible bonds: June 1990 6.50% January-February 1996 4%	June 1990 6.5% bonds were called for redemption, in accordance with the initial issue agreement, in January 1999

* FRF 827 million in capitalization of additional paid-in capital to round up the par-value of shares to EUR 10.

** a minimum of 1.4 million shares still have to be canceled, i.e. nearly 1% of the capital.

Securities not representing an interest in the share capital

Suez Lyonnaise des Eaux has not issued any founder's shares or voting rights certificates.

6.50% convertible bonds issued in June 1990

In June 1990, Lyonnaise des Eaux issued convertible bonds for a total amount of FRF 2,362,992,000. FRF 720 million of these bonds were placed on the international market. 2,953,740 bonds with a FRF 800 par value were issued in all, bearing interest at 6.50%.

In 1998, 141,342 bonds were converted.

In accordance with the Executive Board's deliberation on December 7, 1998, all of these bonds were called for early redemption beginning as of January 4, 1999. They retained their conversion right for a period of three months following the call for redemption, i.e. through April 3, 1999.

As of December 31, 1998, 2,810,358 bonds were outstanding, i.e. 95.2% of the total number of bonds issued.

The bond's highest/lowest prices for 1998 were respectively FRF 1,195.02 (EUR 182.18) and FRF 925.03 (EUR 141.02), closing at FRF 1,133.95 (EUR 172.87) as of December 31, 1998.

4% convertible bonds issued in January-February 1996

In February 1996, Lyonnaise des Eaux issued convertible bonds for a total amount of FRF 3,450,000,320.

A total of 6,634,616 bonds bearing interest at 4% were issued to this end at a par value of FRF 520. These bonds will be redeemed in full on January 1, 2006 at a price of FRF 630, corresponding to 121.15% of the issue price. Based on the current conversion parity, each bond can be converted at any time at the rate of one bond for one share.

In 1998, 75,759 bonds were converted. As of December 31, 1998, 6,558,541 bonds were outstanding, i.e. 98.9% of the total number of bonds issued.

The bond's highest/lowest prices for 1998 were respectively FRF 1,200 (EUR 182.94) and FRF 726 (EUR 110.68), closing at FRF 1,119.72 (EUR 170.70) as of December 31, 1998.

Equity warrants

In June 1996, Northumbrian Water Group Plc, in which Suez Lyonnaise des Eaux has a controlling interest of almost 71% of the capital, issued 69,937,105 shares. A Suez Lyonnaise des Eaux equity warrant was attached to each of these new shares with 35 warrants entitling their holder to subscribe to one Suez Lyonnaise des Eaux share.

The warrants may be exercised at any time during the following period(s):

- during a period of 5 work days starting on the 21st calendar day preceding the day when Northumbrian Water Group Plc shares are expected to be quoted on the London Stock Exchange, provided that this first quotation takes place before December 31, 1999.
- between January 1, 2000 and April 30, 2001 inclusive. After April 30, 2001, any warrants not exercised lose their value. Given the cancellation of 35,759,150 warrants belonging to the former Compagnie de Suez at the time of the merger in June 1997, the maximum number of Suez Lyonnaise des Eaux shares that may be issued through the exercise of these warrants henceforth amounts to 976,513.

As of December 31, 1998, no warrant had been exercised.

For each exercise period, the striking price for warrants will be computed as follows:

- C corresponds to the average of the opening Suez Lyonnaise des Eaux share prices quoted at the Paris Stock Exchange on ten consecutive days of trading during which Suez Lyonnaise des Eaux shares shall have been traded, prior to the day before the first day of the warrant exercise period in question,
- if C is lower than or equal to FRF 800, the warrant striking price will be FRF 540,
- if C is greater than FRF 800, the striking price will amount to:

$$\text{FRF } 540 + \frac{(C\text{-}800)}{2}$$

Guaranteed value certificates (GVCs)

Within the scope of the public offer of exchange with regard to the capital of Société Générale de Belgique that took place in June and July 1998 and in order to remunerate the contribution of 25,396,358 Société Générale de Belgique shares, Suez Lyonnaise des Eaux issued 25,396,358 new shares and 25,396,358 guaranteed value certificates. These guaranteed value certificates entitle holders to receive, between December 29, 2000 and March 30, 2001, a sum in French Francs equal to the difference, if positive, between FRF 1,100 and the listed market price of Suez Lyonnaise des Eaux shares, as defined in the offer of exchange, up to FRF 180 per GVC.

These GVCs have been listed on the Paris Stock Exchange since July 6, 1998. The total volume of transactions, as of March 31, 1998, was 21,340,476 for an average market price of EUR 7.77.

Share subscription plan reserved for Group personnel under employee savings plans

At the Ordinary and Extraordinary General Meeting of Suez Lyonnaise des Eaux on June 11, 1998, the shareholders again authorized the Executive Board to increase the Company's capital by issuing Suez Lyonnaise des Eaux shares reserved for subscription by Group personnel under the terms of employee savings plans, within a limit of 5% of the share capital, as of the date of the Executive Board's decision.

At its meeting on September 14, 1998, the Executive Board took advantage of this authorization and decided to issue an initial 1,000,000 shares at a price of FRF 798 per share. The number of new shares subscribed by employees following this decision was 260,665.

Stock options granted to employees and corporate officers of the Suez Lyonnaise des Eaux Group

In 1998, 417,421 shares with a par value of FRF 60 were issued following the exercise of stock options by employees of the group.

Stock options issued by the companies of the Group

Stock option plans have been implemented in several subsidiaries of the Suez Lyonnaise des Eaux Group.

The stock options of each subsidiary are allocated only to corporate officers and senior executives of the company in question.

Hereafter is a summary of the stock options exercised:

Stock option plans of the former Lyonnaise des Eaux

STOCK OPTION PLANS	STRIKING PRICE (FRF)	NUMBER OF OPTIONEES PER PLAN	TOTAL NUMBER OF SHARES	NUMBER OF SHARES TO BE SUBSCRIBED BY THE MANAGEMENT BOARD	NUMBER OF OPTIONEES (EXECUTIVE BOARD)	STOCK OPTIONS EXERCISED IN 1998	BALANCE CARRIED FORWARD AS OF DEC. 31, 1998	EXPIRY DATE
07/07/1993(1)	430	225	(284,450)	(83,300)	15	214,550	-	07/07/1998
07/15/1994	485	361	338,750	102,100	15	56,480	268,250	07/15/2002
06/14/1995	493	422	366,850	112,200	15	34,200	321,950	06/17/2003
07/24/1996	456	492	454,300	136,000	15	50,550	401,650	07/24/2004
TOTAL			1,159,900	350,300		355,780	991,850	

(1) Plan now expired

Stock option plans of the former Compagnie de Suez

STOCK OPTION PLANS	STRIKING PRICE (FRF)	NUMBER OF OPTIONEES PER PLAN	TOTAL NUMBER OF SHARES	NUMBER OF SHARES TO BE SUBSCRIBED BY THE MANAGEMENT BOARD	NUMBER OF OPTIONEES (EXECUTIVE BOARD)	STOCK OPTIONS EXERCISED IN 1998	BALANCE CARRIED FORWARD AS OF DEC. 31, 1998	EXPIRY DATE
10/12/1993(1)	573.06	57	(62,635)	(10,347)	7	50,106	-	10/12/1998
12/20/1994	433.47	56	83,049	17,427	8	6,535	74,608	12/20/1999
10/15/1996*	321.09	61	87,265	31,279	10	5,158	82,107	10/15/2004
TOTAL			170,314	48,706		61,799	156,715	

* stock purchase plan (for already existing shares)
(1) plan already expired

Stock option plans of Suez Lyonnaise des Eaux

STOCK OPTION PLANS	STRIKING PRICE (FRF)	NUMBER OF OPTIONEES PER PLAN	TOTAL NUMBER OF SHARES	NUMBER OF SHARES TO BE SUBSCRIBED BY THE CORPORATE OFFICERS OF THE GROUP	NUMBER OF OPTIONEES (CORPORATE OFFICERS OF THE GROUP)	STOCK OPTIONS EXERCISED	BALANCE CARRIED FORWARD AS OF DEC. 31, 1998	EXPIRY DATE
11/17/1997	573	873	999,200	176,000	21	5,000	994,200	11/17/2005
11/16/1998*	978	971	1,040,700	247,700	25	0	1,040,700	11/16/2006
TOTAL			2,039,900	423,700		5,000	2,034,900	

* Stock purchase plan (for already existing shares)

STOCK MARKET INFORMATION

The Ordinary and Extraordinary General Meeting of Shareholders on June 11, 1998 authorized the Company to trade in its own shares in order to manage its equity based on conditions set by the laws and regulations that apply.

Conditions: Maximum purchase price FRF 1,200
Minimum selling price FRF 750
Quantity: 10% of the capital

Between August and October 1998, the Company acquired 4,759,580 shares:

- 4,223,082 within the framework of the release from cross-shareholdings with Saint Gobain,
- 535,000 on the market,
- 1,498 from a company of the Group,

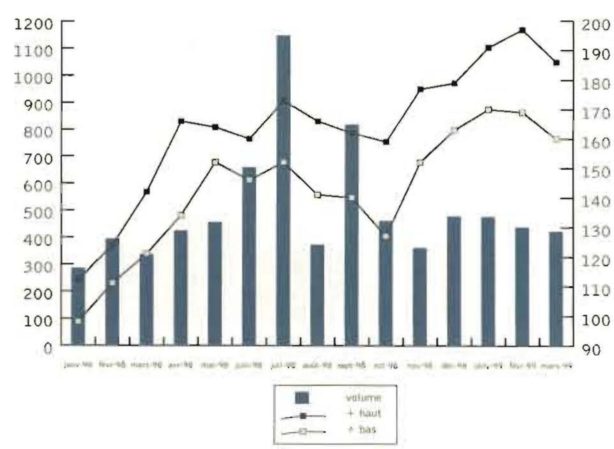
for a total value of FRF 4,786,902,243.40 and a per-share value of FRF 1,005.74. These shares were canceled at the end of October 1998. At the end of March 1998, Suez Lyonnaise des Eaux held 465,156 in treasury stock.

Markets on which the company's securities are listed

Suez Lyonnaise des Eaux shares are listed on the Paris Stock Exchange monthly settlement market and on the Stock Exchanges of Brussels, Luxembourg and Geneva.

As of December 31, 1998, the closing price of the share was FRF 1,148 (EUR 175.01).

Variation in highest and lowest stock exchange prices (in EUR) and average volume of transactions



Traded options on shares

Volume (number of contracts) exchanged for Suez Lyonnaise des Eaux-class options in 1998

Purchase options:	424,587
Selling options:	312,905
TOTAL	737,492

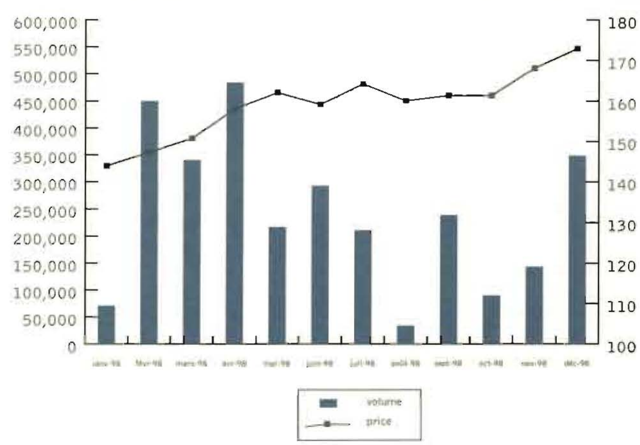
6.50% convertible bonds issued in June 1990

These securities were listed on the *Cote Officielle* (Paris Stock Exchange official list) on July 2, 1990. As of December 31, 1998, the number of potential shares liable to be issued as a result of conversion of the bonds was 2,810,358. All these bonds were called for early redemption starting as of January 4, 1999.

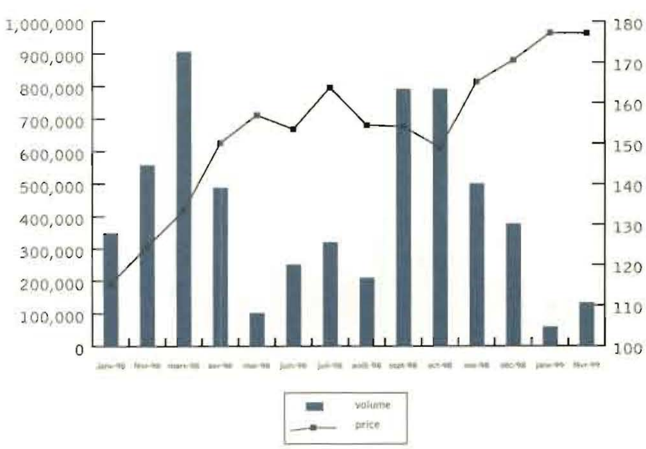
4% convertible bonds issued in January-February 1996

These securities were listed on the *Cote Officielle* (Paris Stock Exchange official list) on February 6, 1996. As of December 31, 1998, the number of potential shares liable to be issued as a result of conversion of the bonds was 6,558,541.

Average stock exchange prices and trading volume relating to June 1990 6.50% convertible bonds



Average stock exchange prices and trading volume relating to January-February 1996 4% convertible bonds



BREAKDOWN OF THE CAPITAL AS OF DECEMBER 31, 1998

The share capital as of December 31, 1998 consisted of 147,767,737 shares with a par value of FRF 60 each, representing 164,039,271 voting rights.

After the conversion of capital into euros, the share capital of Suez Lyonnaise des Eaux was EUR 1,477,677,370, comprising 147,767,737 shares of a par value of EUR 10 each.

Suez Lyonnaise des Eaux carried out an investigation into identifiable bearer securities for clearing in January 1999, which identified around 300,000 shareholders.

Share ownership

Breakdown of main shareholders

	% OF CAPITAL	% OF VOTING RIGHTS*
Electrafina	10.7%	12.6%
Crédit Agricole	6.1%	10.5%
CDC	3.1%	4.4%
Cogema	3.1%	2.8%
Fortis	2.2%	2.0%
CNP Assurances	2.1%	1.9%
AXA	2.0%	1.8%
Treasury stock	1.7%	-
Employees	0.7%	0.7%
Other shareholders	68.3%	63.3%
	100%	**100%**

* Based on our last statement in the *Bulletin des annonces légales obligotoires* (Bulletin of compulsory legal notices) on July 10, 1998, i.e. 163,796, 863 voting rights.

Significant changes in the share ownership over the last three fiscal years

Over the last three fiscal years, the Electrafina holdings in the capital of Suez Lyonnaise des Eaux have increased from 6.1% to 10.7%.

To our knowledge, there is no shareholders' agreement in existence.

Dividends over the last five fiscal years (in FRF)

Fiscal year	Net dividend	Tax credit	Aggregate income
1993	11	5.50	16.50
1994	11.50	5.75	17.25
1995	11.50	5.75	17.25
1996	12	6	18
1997	15	7.50	22.50

Dividends that are not claimed within five years are paid to the French Treasury.

MEMBERS OF THE EXECUTIVE BOARD AND THE SUPERVISORY BOARD

Executive Board

Mr. Gérard Mestrallet
President of the Executive Board

Mr. Philippe Brongniart
Member of the Executive Board

Mr. François Jaclot
Member of the Executive Board

Supervisory Board

Mr. Jérôme Monod
President of the Supervisory Board

Mr. Jean Gandois
Vice-President of the Supervisory Board
Former President of C.NP.F.

Mr. Gerhard Cromme
Chairman of the Executive Board of Thyssen Krupp AG

Viscount Etienne Davignon
Chairman of Société Générale de Belgique

Mr. Paul Desmarais Jr.
Chairman of the Board and Co-Chief Executive
of Power Corporation of Canada

Mr. Reto Domeniconi
Former Executive Vice President of Nestlé S.A. (Switzerland)

Mr. Lucien Douroux
Chief Executive Officer of Caisse Nationale de Crédit Agricole

Mr. Jean Dromer
Chairman of Fondation de France
Deceased on November 24, 1998

Mr. Pierre Faurre
Chairman of Sagem

Mr. Ricardo Fornesa Ribo
Chairman of Sociedad General de Aguas de Barcelona S.A.

Baron Albert Frère
Chairman of Groupe Bruxelles Lambert

Sir Frederick Holliday
Chairman of Northumbrian Water Group

Mr. Philippe Jaffré
Chairman and Chief Executive Officer of Elf Aquitaine

Mr. André Jarrosson
Honorary Chairman of Groupe GTM

Mr. Jacques Lagarde
Advisor to the Chairman of The Gillette Company

Mr. Philippe Malet
Honorary Chairman of Compagnie des Salins du Midi
et des Salines de l'Est

Mr. Bernard Mirat
Former Deputy Chairman and C.E.O. of Société des Bourses
Françaises

Mr. Jean Peyrelevade
Chairman of Crédit Lyonnais

Mr. Claude Pierre-Brossolette
Chairman of Caisse de Refinancement Hypothécaire

Mr. Jean Syrota
Chairman of Cogema

Shares of the members of the Supervisory Board

In accordance with the by-laws, the Members of the Supervisory Board of Suez Lyonnaise des Eaux must each hold at least 400 shares of the Company.

Directors' fees

The amount of the directors' fees paid for the 1998 fiscal year to the members of the Supervisory Board as well as the members of the three committees of the Supervisory Board of Suez Lyonnaise des Eaux was FRF 3,435,000 (an overall annual amount of FRF 3,500,000 was allocated by the Ordinary and Extraordinary General Meeting of Shareholders on June 11, 1998).

Reports of the committees of the Supervisory Board

Audit Committee report

Following the unfortunate death of Jean Dromer on November 24, 1998, Mr. Lucien Douroux was appointed to replace him upon the proposal made by the Remuneration and Nominations Committee at the Supervisory Board Meeting on January 13, 1999.

The Audit Committee is now composed of the following four members: Messrs. Claude Pierre-Brossolette (President), Lucien Douroux, Philippe Jaffre and Bernard Mirat.

The Committee has two primary roles. The first is to carry out a detailed examination of the half-yearly and yearly financial statements in order to clarify to the Supervisory Board their content, their presentation to the public and the changes in the accounting methods. The second is to take note of internal and external control procedures in order to ensure that they cover risk areas adequately.

With respect to the transposition of International Accounting Standards into the accounting standards of the Suez Lyonnaise des Eaux group, the Committee was closely involved in progressively implementing these new international accounting standards. At the end of 1997, fourteen International Accounting Standards were already implemented by the Group. Two new standards were adopted as of the closing on June 30, 1998, taking retroactive effect as of January 1, 1998. One standard pertains to construction contracts and the other pertains to lease agreements, which led to including all the leasing commitments in the balance sheet. With respect to the pension commitments standard, the Committee approved the implementation of this standard in a year's time, so that the calculations of pension commitments for certain foreign subsidiaries may be finalized.

The Committee noted that the Group had undertaken a study to calculate the impact of the changes resulting from the new French methods for consolidated financial statements and that it did not intend to implement these methods ahead of time.

The committee noted that, as the amounts in question were small in relation to net income, there was no reason to change the initial balance sheet of the Lyonnaise des Eaux/Compagnie de Suez merger.

Furthermore, the Committee took note of the changes in the control procedures within the group. The Group's internal audit was organized as a network composed of a central audit (that of the parent company) and local audits for each core business: Water audit (Lyonnaise des Eaux), Energy audit (Elyo), Waste Services audit (Sita) and Construction audit (GTM). Given its size, the Communications division is directly controlled by the central audit function. The structuring of the internal control and audit procedures of the French holding company with those of the Belgian part of the Group will be clarified during the 1999 fiscal year.

The Committee examined the Group's exposure to the risks in emerging countries, particularly within Asia and Latin America, and the steps and options taken to manage these risks.

The Committee validated the action plans undertaken by the Group with respect to the Year 2000 date change and the changeover to the euro, both as regards management IT and technical IT issues. At its meeting on December 21, 1998, the Executive Board, which wanted to have a single Statutory Auditor throughout the chain: Suez Lyonnaise des Eaux - Société Générale de Belgique - Tractebel - Electrabel, decided to propose to the General Meeting of Shareholders the appointment of a third Statutory Auditor, Deloitte Touche Tohmatsu, which is already the Auditor of the three aforementioned major Belgian entities. At the Audit Committee Meeting on March 4, 1999, the proposal was unanimously approved as this appointment would help make methods consistent and facilitate the consolidation of the Group.

Ethics Committee report

The Ethics Committee of Suez Lyonnaise des Eaux's Supervisory Board is composed of Messrs. Jacques Lagarde, Frederick Holliday, André Jarosson and Jean Syrota. Mr. René Coulomb was also a member of the Committee until the General Meeting of Shareholders on June 11, 1998, when he resigned from his position to become Advisor to the President; acting in this capacity, he continued to attend the Committee's meetings. The Committee, which is chaired by Mr. Jacques Lagarde, held three meetings over the year. President Jérôme Monod and President Gérard Mestrallet attended the last meeting at which the Group's Values and Ethics were presented. Over the course of the year, the Committee closely followed the implementation of this Ethics and Values program that consisted of:

- establishing the Values, based on a survey of some 85,000 employees and taking account of the comments of some 10 groups of senior executives from different parts of the world;

- drawing up the Group's Ethics Charter and two implementation documents: Organization Guidelines and Code of Conduct for the Group's Companies and the International Labor Charter. The latter document, co-authored by Messrs. Gérard Mestrallet and Philippe Brongniart, and the employee representatives within the Group's European Dialog Entity, presents the values behind the human resources policy and the rights that are recognized as fundamental rights within the Group.

The Group's Values and Ethics, officially presented to employees on January 5, 1999, are currently being distributed. The Ethics Committee expressed its satisfaction with the work carried out and the values and ethics adopted.

The Committee took note of the more widespread use of letters of compliance that the Presidents of the Group's major companies are required to submit each year to the President of the Executive Board. For the first time, the major holdings of the former Compagnie de Suez implemented this procedure that was used by the former Lyonnaise des Eaux and that the Group adopted at the time of the merger in June 1997.

Environmental issues, risks and prevention were addressed at each meeting; the second meeting focused primarily on these issues. Thus, it was possible to study, in particular, the measures taken in order to strengthen emissions standards for refuse incinerating plants and to study the capacity of the Group's companies to handle crisis situations. The Committee evoked the importance of using awareness/responsibility, training and control actions to complement the environmental strategy, as was done in the area of ethics. It noted that an environmental charter would be drawn up and distributed within the Group in 1999 and would be available on the Internet like the other ethics documents. The Group's views on ethics are shared and disseminated through the involvement of management, functional management networks (Human Resources, Communications, Audit, etc.) and employees. Three seminars were held over the course of the year bringing together 300 Group employees and directors of subsidiaries to reflect on and receive training on their duties and responsibilities.

As required, the Committee noted that the structures and procedures implemented at the parent company level are developing and increasingly being used within the subsidiaries, thus facilitating implementation of all the rules of conduct laid down by the Group.

Compensation and Nominations Committee report

The Compensation and Nominations Committee discussed the amount and terms of the variable portion of the remuneration of the President and the Vice-President of the Supervisory Board as well as the Members of the Executive Board.

As was the practice before the merger in both Lyonnaise des Eaux and Compagnie de Suez, the Committee confirmed that the remuneration of corporate officers should include a substantial portion that is variable. The proportion of the variable portion within the total amount of remuneration stands between 28% and 41%, and the proportion of the variable remuneration increases in relation to the degree of operating responsibility.

The index chosen to determine the variable portion is the Group's share of net current income per share. Each year a target is set that corresponds to the amount of the base variable remuneration; a progression scale for this remuneration is drawn up to make it possible to determine the amount of the variable portion based on the income actually generated, however this amount has a 175% upper limit and a 25% lower limit with respect to the base amount.

Choosing net current income per share as the criterion to set the variable portions made it possible to have a simple tool that is in line with the Group's financial strategy. The Committee is currently considering a second criterion that takes into account the return on the Group's equity.

With respect to stock options, the Committee was informed of the policy implemented by the Executive Board and made proposals to the Supervisory Board regarding the stock options to be allocated to the corporate officers. It gave its approval for the position favoring the number of stock options allotted rather than the average value of the stock options allotted.

The table below shows the number of stock options allotted or shares purchased over the last two fiscal years:

Suez Lyonnaise des Eaux's plans

Stock option plans	Number of optionees	Total number of shares	Number of shares to be subscribed by the corporate officers of the Group	Number of optionees (corporate officers of the Group)
1997	873	999,200	176,000	21
1998	978	1,040,700	247,000	25

(1) The variable portion should correspond to the pre-set target.

INFORMATION ON SUBSIDIARIES AND AFFILIATES AS OF DECEMBER 31,

		CAPITAL	RESERVES AND RETAINED EARNINGS (*)	SHARE OF CAPITAL HELD (AS A PERCENTAGE)
A - Detailed information concerning affiliates whose gross value exceeds 1% of the capital of Suez Lyonnaise des Eaux, i.e. EUR 13,516.30				
I. Subsidiaries (at least 50% of the capital held by Suez Lyonnaise des Eaux)				
Eau et Force - 72, avenue de la Liberté - 92000 Nanterre	C	59.0	343.5	100.0
Société de Contrôle et de Management - 2, rue du Président Carnot - 69293 Lyon	C	16.6	16.0	84.13
Degrémont - 183, avenue du 18 juin 1940 - 92500 Rueil-Malmaison	C	56.7	54.1	95.15
DBLE - 72, avenue de la Liberté - 92000 Nanterre	C	0.9	4.4	99.95
Sita - 94, rue de Provence - 75009 Paris	C	86.1	1,128.6	50.65
Elyo - 235, avenue Georges Clémenceau - 92000 Nanterre	C	207.8	369.5	100.00
Hungariaviz - H-1134 Budapest Vaci ut 23-27 - 1566 Budapest - Hungary		6,000	844	51.00
Dumez - 32, avenue Pablo Picasso - 92000 Nanterre	C	116.6	(21.6)	100.00
Fided - 32, avenue Pablo Picasso - 92000 Nanterre	C	245.3	30.0	90.11
Ogelye - 72, avenue de la Liberté - 92000 Nanterre	C	50.3	(50.3)	100.00
Lyonnaise American Holding - 100 West Tenth St-Wilmington - 19801 Delaware-USA	C	208	6	100.00
Hisusa - 110, principe de Vergara - Madrid 28002 - Spain	C	138.2	319.8	51.00
Lyonnaise Europe PLC - Mildmay road - Chelmsford - Essex CM 0XW - UK	C	419	18	80.00
Lyonnaise des Eaux Canada - 8200 bd Decaric - Montreal - Quebec H4P 2P5 - Canada	C	68	7	51.35
Aguas Provinciales de Santa Fe - calle 9 de Julio - Santa Fe - Argentina	C	60	7	51.69
Pam Lyonnaise Jaya - sentral Senayan 1 - office tower Lantai 7 - Jalan Asia Afrika n 8 - Jakarta Pusai 10270 - Indonesia	C	105,000	(66,394)	100.00
Lyonnaise Communication - 4-6, villa Thoréton - 75015 Paris	C	29.4	17.7	76.77
S.S.I.M.I - 72, avenue de la Liberté - 92000 Nanterre	C	144.7	(0.2)	100.00
Auxipar - 72, avenue de la Liberté - 92000 Nanterre	C	57.3	9.0	100.00
Suez Industrie - 68, rue du Faubourg Saint-Honoré - 75008 Paris	C	113.7	346.8	100.00
Frabepar - rue Blanche 27 - 1050 Brussels - Belgium	C	4.2	423.2	100.00
Findim (formerly Crédisuez) - 1, rue d'Astorg - 75008 Paris	C	303.2	(290.6)	100.00
Banque Sofinco - Rue du Bois Sauvage - 91038 Evry cedex	C	113.1	264.7	99.98
Sopranor - 4, place des Saussaies - 75008 Paris	C	0.2	85.4	99.90
Société Financière d'Epargne - 4, place des Saussaies - 75008 Paris	C	29.0	76.4	100.00
La Hénin Vie - 14, rue Roquépine - 75379 Paris 08	C	46.0	62.2	68.30
Société Générale de Belgique - rue Royale 30 - 1000 Brussels - Belgium	C	1,460.8	4,750.3	90.53
Auxilex - 4, place des Saussaies - 75008 Paris	C	31.9	41.8	100.00
II. Affiliates (10% to 50% of the capital held by Suez Lyonnaise des Eaux)				
Lydec - 20, Boulevard Rachidi - Casablanca - Morocco	C	800	(290)	35.00
Aguas Argentinas - Reconquite 823 CP - 1003 Buenos Aires - Argentina	C	159	133	35.59
Maynilad Water Services - 4 th floor, Benpres Building. Meralco ave - Pasig City - Philippines		1,800	(547)	20.00
Métropole Télévision - 89, avenue Charles de Gaulle - 92200 Neuilly-sur-Seine cedex	C	40.2	187.4	34.46

C = consolidated companies
* before allocation of the income of the fiscal year, including investment subsidies, premiums, and statutory provisions.
(1) these figures are given in EUR millions, for foreign subsidiaries as well.

1998

In millions of EUR, unless otherwise stated

Book value of shares held Gross (1)	Net (1)	Loans and advances granted but not yet repaid (1)	Amount of guarantees and surety given by the company	Revenues (losses) From the second to last fiscal year	From the last fiscal year	Profits (losses) from the second to last fiscal year	rom the last fiscal year	Dividends collected by the company during the fiscal year (1)	Remarks
408.6	408.6			309.5	345.0	13.0	8.8	2.4	
250.8	250.8			2.1	2.0	4.0	2.3	3.4	
190.7	190.7			304.0	333.1	(13.0)	5.4	9.8	
39.9	39.9			-	-	1.1	0.5	1.1	
374.7	374.7	63.1		41.8	21.6	24.2	172.7	9.5	
608.0	608.0			378.5	564.8	(4.3)	(7.6)	-	
14.0	13.1	3.0	62.7	-	1,934	(11)	855	-	In millions of Hungarian forints
346.5	127.0			5.6	4.3	17.2	37.2	-	
371.1	359.5	5.9		-	-	6.9	8.2	7.9	
50.3	50.3	29.0		-	-	(14.6)	(35.5)	-	
193.9	193.9			-	-	23	7	29.7	In millions of U.S. dollars
101.5	101.5			-	-	25.2	27.3	13.9	
508.3	508.3		18.4	-	-	25	35	30.5	In millions of Pounds sterling
25.0	21.5			-	-	4	27	6.7	In millions of Canadian dollars
37.5	37.5		84.2	82	87	6	5	-	In millions of Argentinean pesos
24.1	4.1	10.2	8.5	-	179,467	-	(49,463)	-	In millions of Indonesian rupiahs
53.2	53.2	1.7		28.7	49.4	(4.9)	25.8	-	
228.5	149.7	12.7		20.4	22.7	(30.0)	6.6	-	
76.4	76.4	15.4		-	-	(2.9)	(2.4)	-	
512.8	512.8		35.8	-	-	60.5	89.0	114.3	
456.1	456.1			-	-	19.1	19.6	18.6	
2,822.3	1,229.5		240.9	80.6	101.7	(625.5)	(290.6)	-	
162.4	162.4			789.1	611.0	76.7	72.0	38.4	
289.7	70.9			-	-	5.8	12.7	4.0	
77.4	77.4			-	-	41.0	2.6	15.9	
49.2	46.8			854.5	631.0	6.9	8.1	2.6	
6,312.5	6,312.5			-	1,231.1	561.2	2,573.3	114.5	
32.3	32.3	0.3		-	-	1.7	10.7	2.0	
26.7	16.9		3.2	1,421	3,533	(130)	(161)	-	In millions of Moroccan dirhams
102.3	102.3		242.4	433	460	58	37	27.0	In millions of Argentinean pesos
16.3	7.8		20.6	732	1,724	(350)	(547)	-	In millions of Philippine pesos
124.7	124.7			339.8	386.0	75.9	91.0	20.3	

INFORMATION ON SUBSIDIARIES AND AFFILIATES AS OF DECEMBER 31,

		CAPITAL	RESERVES AND RETAINED EARNINGS (*)	SHARE OF CAPITAL HELD (AS A PERCENTAGE)
III. Other investments in subsidiaries and affiliates				
(less than 10% of the capital held by Suez Lyonnaise des Eaux)				
AXA - 9, place Vendôme - 75001 Paris		3,204.0	10,333.1	1.23
Northumbrian Water Group - P.O. Box 4, Gosforth - Newcastle Upon Tyne NE3 3PX - UK	C	123	844	7.67
Groupe GTM - 61, avenue Jules Quentin - 92003 Nanterre cedex	C	116.5	368.5	4.69
Sociedad General de Aguas de Barcelona - paseo de San Juan 39 - 08009 Barcelona - Spain	C	137.3	666.0	1.46
B - Global information concerning other subsidiaries or affiliates				
I. Subsidiaries not included in paragraph A				
a) French subsidiaries - combined				
a) Foreign subsidiaries - combined				
II. Affiliates not included in paragraph A				
a) French companies - combined				
a) Foreign subsidiaries - combined				

C = consolidated companies

* before allocation of the income of the fiscal year, including investment subsidies, premiums, and statutory provisions.

(1) these figures are given in EUR millions, for foreign subsidiaries as well.

1998

In millions of EUR, unless otherwise stated

Book value of shares held Gross (1)	Net (1)	Loans and advances granted but not yet repaid (1)	Amount of guarantees and surety given by the company	Revenues (losses) From the second to last fiscal year	From the last fiscal year	Profits (losses) from the second to last fiscal year	rom the last fiscal year	Dividends collected by the company during the fiscal year (1)	Remarks
336.3	269.2			55,587.2	56,697.5	1,207.4	1,530.9	5.9	
64.0	64.0			-	562	54	135	4.1	In millions of Pounds sterling
43.8	42.7			41.0	38.0	(7.9)	9.3	0.8	
20.1	20.1			1,179.6	1,525.9	71.6	87.5	0.3	
47.9	35.4	145.1	-					10.5	
38.9	14.9	43.1	48.5					5.2	
30.6	26.4	8	47.0					16.9	
79.1	74.7	(c*)15.0	34.8					4.3	(c *) of which preference shares: 14.9

INFORMATION ON SUBSIDIARIES AND AFFILIATES AS OF DECEMBER 31,

		CAPITAL	RESERVES AND RETAINED EARNINGS (*)	SHARE OF CAPITAL HELD (AS A PERCENTAGE)
A - Detailed information concerning affiliates whose gross value exceeds 1% of the capital of Suez Lyonnaise des Eaux, i.e. FRF 88,660,642				
I. Subsidiaries (at least 50% of the capital held by Suez Lyonnaise des Eaux)				
Eau et Force - 72, avenue de la Liberté - 92000 Nanterre	C	387	2,253	100.00
Société de Contrôle et de Management - 2, rue du Président Carnot - 69293 Lyon	C	109	105	84.13
Degrémont - 183, avenue du 18 juin 1940 - 92500 Rueil-Malmaison	C	372	355	95.15
DBLE - 72, avenue de la Liberté - 92000 Nanterre	C	6	29	99.95
Sita - 94, rue de Provence - 75009 Paris	C	565	7,403	50.65
Elyo - 235, avenue Georges Clémenceau - 92000 Nanterre	C	1,363	2,424	100.0
Hungariaviz - H-1134 Budapest Vaci ut 23-27 - 1566 Budapest - Hungary		6,000	844	51.00
Dumez - 32, avenue Pablo Picasso - 92000 Nanterre	C	765	(142)	100.0
Fided - 32, avenue Pablo Picasso - 92000 Nanterre	C	1,069	197	90.11
Ogelye - 72, avenue de la Liberté - 92000 Nanterre	C	330	(330)	100.00
Lyonnaise American Holding - 100 West Tenth St-Wilmington - 19801 Delaware-USA	C	208	6	100.00
Hisusa - 110, principe de Vergara - Madrid 28002 - Spain	C	22,998	53,211	51.00
Lyonnaise Europe PLC - Mildmay road - Chelmsford - Essex CM 0XW - UK	C	419	18	80.00
Lyonnaise des Eaux Canada - 8200 bd Decaric - Montreal - Quebec H4P 2P5 - Canada	C	68	7	51.35
Aguas Provinciales de Santa Fe - calle 9 de Julio - Santa Fe - Argentina	C	60	7	51.69
Pam Lyonnaise Jaya - sentral Senayan 1 - office tower Lantai 7 - Jalan Asia Afrika n 8 - Jakarta Pusai 10270 - Indonesia	C	105,000	(66,394)	100.00
Lyonnaise Communication - 4-6, villa Thoréton - 75015 Paris	C	193	116	76.77
S.S.I.M.I - 72, avenue de la Liberté - 92000 Nanterre	C	949	(1)	100.00
Auxipar - 72, avenue de la Liberté - 92000 Nanterre	C	376	59	100.00
Suez Industrie - 68, rue du Faubourg Saint-Honoré - 75008 Paris	C	746	2,275	100.00
Frabepar - rue Blanche 27 - 1050 Brussels - Belgium	C	171	17,070	100.00
Findim (formerly Crédisuez) - 1, rue d'Astorg - 75008 Paris	C	1,989	(1,906)	100.00
Banque Sofinco - Rue du Bois Sauvage - 91038 Evry cedex	C	742	1,736	99.98
Sopranor - 4, place des Saussaies - 75008 Paris	C	1	560	99.90
Société Financière d'Epargne - 4, place des Saussaies - 75008 Paris	C	190	501	100.00
La Hénin Vie - 14, rue Roquépine - 75379 Paris 08	C	302	408	68.30
Société Générale de Belgique - rue Royale 30 - 1000 Brussels - Belgium	C	58,929	191,628	90.53
Auxilex - 4, place des Saussaies - 75008 Paris	C	209	274	100.00
II. Affiliates (10% to 50% of the capital held by Suez Lyonnaise des Eaux)				
Lydec - 20, Boulevard Rachidi - Casablanca - Morocco	C	800	(290)	35.00
Aguas Argentinas - Reconquite 823 CP - 1003 Buenos Aires - Argentina	C	159	133	35.59
Maynilad Water Services - 4 th floor, Benpres Building, Meralco ave - Pasig City - Philippines		1,800	(547)	20.00
Métropole Télévision - 89, avenue Charles de Gaulle - 92200 Neuilly-sur-Seine cedex	C	264	1 229	34.46

C = consolidated companies

* before allocation of the income of the fiscal year, including investment subsidies, premiums, and statutory provisions.

(1) these figures are given in FRF millions, for foreign subsidiaries as well.

1998

In millions of FRF, unless otherwise stated

Book value of shares held Gross (1)	Net (1)	Loans and advances granted but not yet repaid (1)	Amount of guarantees and surety given by the company	Revenues (losses) From the second to last fiscal year	From the last fiscal year	Profits (losses) from the second to last fiscal year	rom the last fiscal year	Dividends collected by the company during the fiscal year (1)	Remarks
2,680	2,680			2,030	2,263	85	58	16	
1,645	1,645			14	13	26	15	22	
1,251	1,251			1,994	2,185	(85)	36	64	
262	262			-	-	7	3	7	
2,458	2,458	414		274	142	159	1,133	62	
3,988	3,988			2,483	3,705	(28)	(50)	-	
92	86	20	411	-	1,934	(11)	855	-	In millions of Hungarian forints
2,273	833			37	28	113	244	-	
2,434	2,358	39		-	-	45	54	52	
330	330	190		-	-	(96)	(233)	-	
1,272	1,272			-	-	23	7	195	In millions of U.S. dollars
666	666			-	-	4,187	4,548	91	In millions of Spanish pesetas
3,334	3,334		121	-	-	25	35	200	In millions of Pounds sterling
164	141			-	-	4	27	44	In millions of Canadian dollars
246	246		552	82	87	6	5	-	In millions of Argentinean pesos
158	27	67	56	-	179,467	-	(49,463)	-	In millions of Indonesian rupiahs
349	349	11		188	324	(32)	169	-	
1,499	982	83		134	149	(197)	43	-	
501	501	101		-	-	(19)	(16)	-	
3,364	3,364		235	-	-	397	584	750	
2,992	2,992			-	-	769	792	122	In millions of Belgian francs
18,513	8,065		1,580	529	667	(4,103)	(1,906)	-	
1,065	1,065			5,176	4,008	503	472	252	
1,900	465			-	-	38	83	26	
508	508			-	-	269	17	104	
323	307			5,612	4,139	45	53	17	
41,407	41,407			-	49,661	22,640	103,886	751	In millions of Belgian francs
212	212	2		-	-	11	70	13	
175	111		21	1,421	3,533	(130)	(161)	-	In millions of Moroccan dirhams
671	671		1,590	433	460	58	37	177	In millions of Argentinean pesos
107	51		135	732	1,724	(350)	(547)	-	In millions of Philippine pesos
818	818			2,229	2,532	498	597	133	

Information on subsidiaries and affiliates as of December 31,

		Capital	Reserves and retained earnings (*)	Share of capital held (as a percentage)
III. Other investments in subsidiaries and affiliates				
(less than 10% of the capital held by Suez Lyonnaise des Eaux)				
AXA - 9, place Vendôme - 75001 Paris		21,017	67,781	1.23
Northumbrian Water Group - P.O. Box 4, Gosforth - Newcastle Upon Tyne NE3 3PX - UK	C	123	844	7.67
Groupe GTM - 61, avenue Jules Quentin - 92003 Nanterre cedex	C	764	2,417	4.69
Sociedad General de Aguas de Barcelona - paseo de San Juan 39 - 08009 Barcelona - Spain	C	22,845	110,821	1.46

B - Global information concerning other subsidiaries or affiliates

I. Subsidiaries not included in paragraph A

a) French subsidiaries - combined

a) Foreign subsidiaries - combined

II. Affiliates not included in paragraph A

a) French companies - combined

a) Foreign companies - combined

C = consolidated companies

* before allocation of the income of the fiscal year, including investment subsidies, premiums, and statutory provisions.

(1) these figures are given in FRF millions, for foreign subsidiaries as well.

1998

In millions of FRF, unless otherwise stated

Book value of shares held Gross (1)	Net (1)	Loans and advances granted but not yet repaid (1)	Amount of guarantees and surety given by the company	Revenues (losses) From the second to last fiscal year	From the last fiscal year	Profits (losses) from the second to last fiscal year	rom the last fiscal year	Dividends collected by the company during the fiscal year (1)	Remarks
2,206	1,766			364,628	371,911	7,920	10,042	39	
420	420			-	562	54	135	27	In millions of Pounds sterling
287	280			269	249	(52)	61	5	
132	132			196,264	253,889	11,908	14,565	2	In millions of Spanish pesetas
314	232	952	-					69	
255	98	283	318					34	
201	173	55	308					111	
519	490	(c*)99	228					28	(c *) of which preference shares: 98

TOTAL AND PARTIAL DISPOSALS WHETHER THIS INVOLVES CROSSING THRESHOLDS OR NOT

In EUR Companies	% as of Dec. 31, 1997	% as of Dec. 31, 1998	Reclassification within the group	Disposal outside the group	Book value of securities held as of Dec. 31, 1998 Gross	Net	Business sector
Subsidiaries (over 50% of the capital)							
Urbana	50.00	-		X			Holdings
Sociedad Operadora Grupo Lyonnaise des Eaux	99.76	-	X				Water
Aurépar	99.89	-	Winding-up				Industrial and retail financial
Stralex	99.80	-	X				Industrial and retail financial
Céfina	99.80	-		X			Industrial and retail financial
Sofidim	76.00	-		X			Industrial and retail financial
Spérans	99.68	-	X				Industrial and retail financial
Parsival	99.76	-	Winding-up				Industrial and retail financial
Aurival	99.88	-	Winding-up				Industrial and retail financial
Suez Investment Services	100.00		Liquidation				Industrial and retail financial
Affiliates (over one-third of the capital)							
Suliroc	40.00	-	Winding-up				Industrial and retail financial
Suez loisirs	33.98	-	Winding-up				Miscellaneous
Electricité de Tahiti (EDT)	39.81	-	X				Energy
Vodarny Kanal. Karlovy Vary	49.78	47.76		X	2,739,203.6	2,739,203.6	Water
Affiliates (over 20% of the capital)							
Néant							
Affiliates (over 10% of the capital)							
Fovarosi Vismuvek	12.75	0.87	X		2,822,231.3	2,154,199.7	Water
Maynilad water services	37.50	20.00	X		16,245,773.4	7,838,330.0	Water
Filmarec	20.00	-		X			Industrial and retail financial

NEW SUBSIDIARIES AND AFFILIATES WHETHER THIS INVOLVES CROSSING THRESHOLDS OR NOT

In EUR Companies	% as of Dec. 31, 1997	% as of Dec. 31, 1998	Reclassification within the group	Acquisition outside the group	Book value of securities held as of Dec. 31, 1998 Gross	Net	Business sector
Subsidiaries (over 50% of the capital)							
Suez Lyonnaise des Eaux do Brasil	-	100.00	Incorporation		16,005.3	16,005.3	Water
Aguas de Santa Fe	32.82	51.69		X	37,538,057.6	37,538,057.6	Water
Pam Lyonnaise Jaya	40.00	100.00		X	24,041,228.6	4,119,919.4	Water
Antsu Antalya AS	50.00	100.00		X	365,210.4	0.0	Water
Lyonnaise do Brasil	-	100.00	Incorporation		280,353.7	280,353.7	Water
Affiliates (over one-third of the capital)							
Métropole Télévision	33.15	34.46	X		124,683,872.0	124,683,872.0	Communications
Aguas Argentinas	25.00	35.59		X	102,254,287.9	102,254,287.9	Water
Aguas de Cordobesas	28.89	37.45		X	10,695,197.7	10,122,356.3	Water
P.T.S.S.	-	50.00		X	2,176,972.0	538,145.0	Water
Aquapur	-	48.00		X	1,266.5	1,266.5	Water
Affiliates (over 20% of the capital)							
Lyonnaise Latin Amer. Water corp		25.81	Incorporation		337,083.1	337,083.1	Water
Affiliates (over 10% of the capital)							
None							

TOTAL AND PARTIAL DISPOSALS WHETHER THIS INVOLVES CROSSING THRESHOLDS OR NOT

In FRF

Companies	% as of Dec. 31, 1997	% as of Dec. 31, 1998	Reclassification within the group	Disposal outside the group	Book value of securities held as of Dec. 31, 1998 Gross	Net	Business sector
Subsidiaries (over 50% of the capital)							
Urbana	50.00	-		X			Holding
Sociedad Operadora Grupo Lyonnaise des Eaux	99.76	-	X				Water
Aurépar	99.89	-	Winding-up				Industrial and retail financial
Stralex	99.80	-	X				Industrial and retail financial
Céfina	99.80	-		X			Industrial and retail financial
Sofidim	76.00	-		X			Industrial and retail financial
Spérans	99.68	-	X				Industrial and retail financial
Parsival	99.76	-	Winding-up				Industrial and retail financial
Aurival	99.88	-	Winding-up				Industrial and retail financial
Suez Investment Services	100.00		Liquidation				Industrial and retail financial
Affiliates (over one-third of the capital)							
Suliroc	40.00	-	Winding-up				Industrial and retail financial
Suez loisirs	33.98	-	Winding-up				Miscellaneous
Electricité de Tahiti (EDT)	39.81	-	X				Energy
Vodarny Kanal. Karlovy Vary	49.78	47.76		X	17,967,998	17,967,998	Water
Affiliates (over 20% of the capital)							
None							
Affiliates (over 10% of the capital)							
Fovarosi Vismuvek	12.75	0.87	X		18,512,624	14,130,624	Water
Maynilad water services	37.50	20.00	X		106,565,288	51,416,074	Water
Filmarec	20.00	-		X			Industrial and retail financial

NEW SUBSIDIARIES AND AFFILIATES WHETHER THIS INVOLVES CROSSING THRESHOLDS OR NOT

In FRF

Companies	% as of Dec. 31, 1997	% as of Dec. 31, 1998	Reclassification within the group	Acquisition outside the group	Book value of securities held as of Dec. 31, 1998 Gross	Net	Business sector
Subsidiaries (over 50% of the capital)							
Suez Lyonnaise des Eaux do Brasil	-	100.00	Incorporation		104,988	104,988	Water
Aguas de Santa Fe	32.82	51.69		X	246,233,516	246,233,516	Water
Pam Lyonnaise Jaya	40.00	100.00		X	157,700,122	27,024,900	Water
Antsu Antalya AS	50.00	100.00		X	2,395,623	0	Water
Lyonnaise do Brasil	-	100.00	Incorporation		1,839,000	1,839,000	Water
Affiliates (over one-third of the capital)							
Métropole Télévision	33.15	34.46	X		817,872,586	817,872,586	Communications
Aguas Argentinas	25.00	35.59		X	670,744,160	670,744,160	Water
Aguas de Cordobesas	28.89	37.45		X	70,155,898	66,398,305	Water
P.T.S.S.	-	50.00		X	14,280,000	3,530,000	Water
Aquapur	-	48.00		X	8,308	8,308	Water
Affiliates (over 20% of the capital)							
Lyonnaise Latin Amer. Water corp		25.81	Incorporation		2,211,120	2,211,120	Water
Affiliates (over 10% of the capital)							
None							

TAX INFORMATION RELATING TO THE PARENT COMPANY ACCOUNTS

ACCOUNTS AS OF DECEMBER 31, 1998	AMOUNT (IN FRF)	AMOUNT (IN EUR)
Total non-tax deductible expenses (Article 39-4 of the French Tax Code)	1,210,024	184,467
Total non-tax deductible directors' fees (Article 210 *sexies* of the French Tax Code)	225,954	34,447
Total expenses reported on the special overheads return (Article 223 *quinquies* of the French Tax Code) =		
• Compensation and other expenses relating to the highest-paid employees	38,374,216	5,850,111.5
• Gifts and entertainment	27,487,630	4,190,462.2
• Amount of above expenses added back to taxable income	-	-

INFORMATION REQUIRED UNDER LABOR LAW

Copies of the report on size of the workforce and conditions of employment required under Article L 438-1 *et seq.* of the French Labor Code are available to shareholders on request.

RESPONSIBILITY FOR FINANCIAL INFORMATION AND AUDITING

Persons responsible for the annual report

To the best of our knowledge, the information provided in this document is accurate and includes all necessary data to enable the investors to assess the assets, business activities, financial position, results and future prospects of Suez Lyonnaise des Eaux; no information likely to affect the interpretation of such data has been omitted.

Gérard Mestrallet
President of the Executive Board

Principal statutory auditors

Barbier Frinault et Autres
Appointed: Annual General Meeting, June 14, 1995
Expiry date of term of office: 2001
Annual General Meeting with regard
to the year 2000 accounts
Represented by:
Christian Chochon

Mazars et Guérard
Appointed: Annual General Meeting, June 14, 1995
Expiry date of term of office: 2001
Annual General Meeting
with regard to the year 2000 accounts
Represented by:
Frédéric Allilaire

Deputy statutory auditors

Francis Scheidecker
Appointed: Annual General Meeting, June 14, 1995
Expiry date of term of office: 2001
Annual General Meeting with regard
to the year 2000 accounts

José Marette
Appointed: Annual General Meeting, June 14, 1995
Expiry date of term of office: 2001
Annual General Meeting with regard
to the year 2000 accounts

We have audited the financial and accounting data provided in this annual report, performing such procedures as we have deemed necessary in accordance with generally accepted auditing standards.
Unqualified audit opinions have been issued in respect of the parent company accounts and consolidated financial statements for the 1996, 1997 and 1998 fiscal years.
We have no comments to make on the fair presentation of, or the true and fair view given by, the financial and accounting information presented.
Without qualifying the opinion expressed above, we wish to draw your attention to Notes D and N of the notes to the consolidated financial statements for the 1998 fiscal year which set out your Group's position in relation to the preferred methods recommended by the French National Accounting Institute in terms of leasing and retirement indemnities and pensions.

Barbier Frinault et Autres
41, rue Ybry
92576 Neuilly-sur-Seine cedex
Christian Chochon

Mazars et Guérard
125, rue de Montreuil
75011 Paris
Frédéric Allilaire

Allilaire.

The Statutory Auditors
Members of the Paris and Versailles Regional Institutes

COB

This annual report was registered on May 3, 1999, under the number R.99-157, with the COB (French Securities and Exchange Commission). It may only be used to support a financial transaction if it is supplemented by an official memorandum approved by said Commission.

C.O.B. (FRENCH SECURITIES AND EXCHANGE COMMISSION) TABLE OF EQUIVALENCE

AGENDA

A. Deliberating as an Ordinary General Shareholders' Meeting

- Executive Board's management report
- Supervisory board report
- Statutory Auditors' reports
- Approval of the operations of the 1998 fiscal year and the parent company accounts as of December 31, 1998
- Appropriation of the results and determination of the dividend amount
- Vote on the special report of the Statutory Auditors
- Presentation of the consolidated financial statements as of December 31, 1998
- Renewal of the term of office of a member of the Supervisory Board
- Appointment of a principal statutory auditor and a deputy statutory auditor
- Authority to be vested in the Executive Board for the purpose of trading in company shares
- Authority to be vested in the Executive Board for the purpose of issuing bonds and debt securities

B. Deliberating as an Extraordinary General Shareholders' Meeting

- Executive Board's report
- Special report of the Statutory Auditors
- Reports of the Appraisers of Capital Contributions
- Independent Expert's Report
- Amendment of Article 34 of the by-laws relating to the method of voting
- Authority to be given to the Executive Board for the purpose of increasing the share capital, either by the issue, with maintenance of preferential subscription rights, of shares, warrants and/or marketable securities which give access, immediately or in the long term, to company shares or by the capitalization of premiums, reserves, profits or suchlike
- Authority to be given to the Executive Board for the purpose of increasing the share capital by the issue, with elimination of preferential subscription rights, of shares, warrants and/or marketable securities which give access, immediately or in the long term, to Company shares, including for the purpose of remunerating securities transferred to the Company in the context of a public offer of exchange
- Authority to be given to the Executive Board for the purpose of using the authorizations to increase share capital at the time of a public offer of exchange relating to company securities
- Authority to be given to the Executive Board for the purpose of reducing share capital by canceling shares
- Authority to be given to the Executive Board for the purpose of increasing share capital in favor of Spring Multiple 99 SCA
- Approval of the planned merger-absorption by Suez Lyonnaise des Eaux of Auxilex, a French *société anonyme* (joint-stock corporation) with capital of FRF 209,000,000 having its registered office at: 4, place des Saussaies, 75008 Paris, France, registered with the Commercial and Companies Registry of Paris under the number 712 010 867 RCS Paris; consequently, approval of contributions and their valuation
- Determination and allocation of the merger surplus; reduction in the capital by cancellation of shares held by Auxilex
- Approval of the planned merger-absorption by Suez Lyonnaise des Eaux of Société Financière d'Epargne, a French *société par actions simplifiée* (simplified joint-stock company), with capital of FRF 190,000,000, having its registered office at: 4, place des Saussaies, 75008 Paris, France, and registered with the Commercial and Companies Registry of Paris under the number 341 970 416 RCS Paris; consequently, approval of the contributions and their valuation
- Determination and allocation of the merger surplus; reduction in capital by cancellation of shares held by Société Financière d'Epargne
- Approval of the planned merger-absorption by Suez Lyonnaise des Eaux of DBLE, a French *société anonyme* (joint-stock corporation) with capital of FRF 6,000,000, having its registered office at: 72, avenue de la Liberté, 92000 Nanterre, France, and registered with the Commercial and Companies Registry of Nanterre under the number 338 512 353 RCS Nanterre; consequently, approval of the contributions and their valuation
- Determination and allocation of the merger deficit
- Allocation to the "Additional paid-in capital" item
- Powers for formalities

Executive Board's report

1. Executive Board's report to the Ordinary General Shareholders' Meeting

Approval of the parent company accounts (first resolution)

The General Meeting is asked to approve the operations and parent company accounts for the 1998 fiscal year as they are presented.

Appropriation of net income and determination of the amount of the dividend (second resolution)

	EUR	FRF
in view of retained earnings for the previous fiscal year	4,647,387.49	30,484,863.53
and the profits of the fiscal year closed	691,151,531.51	4,533,656,851.54
total net income to be appropriated amounts to	695,798,919.00	4,564,141,715.07
The Executive Board proposes the following allowances		
• Special long-term capital gains reserve	98,031,901.19	643,047,118.10
• Payment of the dividend to 147,767,737 shares	398,972,889.90	2,617,090,599.40
• *Précompte mobilier* (special equalization tax)	128,015,521.25	839,726,772.70
• Retained earnings	70,778,606.66	464,277,224.87
	695,798,919.00	4,564,141,715.07

If the Meeting approves this proposal, the net dividend for the 1998 fiscal year will be set at EUR 2.70 (FRF 17.71) per share, to which a tax credit of EUR 1.35 (FRF 8.85) will be added, giving total revenue per share of EUR 4.05 (FRF 25.56).

Agreements referred to under Articles 101 and 143 of the Law of July 24, 1966 (third resolution)

The special report of the Statutory Auditors relates to the agreements referred to under Articles 101 and 143 of the Law of July 24, 1966 relating to business corporations.

The special report of the Statutory Auditors on regulated agreements is included on page 58 in this annual report.

The agreements entered into during the 1998 fiscal year are not of an extraordinary nature, with the exception of the agreement entered into with Compagnie de Saint Gobain with a view to releasing cross-shareholdings.

Moreover, since December 31, 1998, several regulated agreements have been entered into:

- In February 1999, the Supervisory Board authorized the sale of Suez Lyonnaise des Eaux's minority interest in Banque Chabrières to the Caisse Nationale de Crédit Agricole
- On March 31, 1999 the Supervisory Board authorized:
  - The sale of 100% of Elyo's capital to Société Générale de Belgique.
  - The purchase from Société Générale de Belgique of its 20% shareholding in Coficem, the holding company controlling Sagem.

Consolidated financial statements (fourth resolution)

It is proposed that the General Meeting review the consolidated financial statements as of December 31, 1998.

The Supervisory Board (fifth resolutions)

The Supervisory Board was deeply saddened by the sudden passing of Mr. Jean Dromer, President of Fondation de France in November 1998. He had participated actively and steadfastly in the Board's work as a long-standing Director of Lyonnaise des Eaux, then as a member of Suez Lyonnaise des Eaux's Supervisory Board as from June 1997.

In addition, in accordance with the provisions of Article 16 of the by-laws relating to the age limit for members of the Supervisory Board, the terms of office of Messrs. Albert Frère, Philippe Malet, and Bernard Mirat expire at this meeting. Messrs. Malet and Mirat are not seeking the renewal of their terms of office.

The board wishes to pay tribute to Mr. Malet, former President of Compagnie Suez and Vice-President of Lyonnaise des Eaux, for his invaluable assistance in the Board's decisions, and to Mr. Mirat for his effective work as adviser responsible for shareholder relations.

It is proposed that the General Meeting renew the term of office of Mr. Albert Frère for one year. His term of office will come to an end at the close of the Ordinary General Meeting which will deliberate on the accounts for the 1999 fiscal year.

Statutory Auditors (sixth and seventh resolutions)

It is proposed that the General Meeting appoint:

• Deloitte Touche Tohmatsu-Audit as principal statutory auditor for six fiscal years.

This firm's term of office will expire at the close of the Ordinary General Meeting which will deliberate on the accounts for the 2004 fiscal year.

- Bureau d'etudes administratives sociales et comptables "BEAS" as deputy Statutory Auditor for six fiscal years.

This firm's term of office will expire at the close of the Ordinary General Meeting which will deliberate on the accounts for the 2004 fiscal year.

Authority to trade in the Company's shares on the Stock Exchange (eighth resolution)

The Ordinary and Extraordinary General Meeting of shareholders on June 11, 1998 authorized the company to trade in the Company's shares on the stock exchange under the following conditions:

- Maximum purchase price: FRF 1,200
- Minimum selling price: FRF 750
- The purchase authorization relates to 10% of the shares in the company's capital.

Between August and October 1998, the company acquired 4,759,580 shares:

- 4,223,082 within the scope of the release from cross-shareholdings with Saint Gobain,
- 535,000 on the market,
- 1,498 from a company within the Group,

for an overall value of FRF 4,786,902,243.40 and a unit value of FRF 1,005,74.

At its meeting on October 26, 1998, the Executive Board decided, with effect from October 30, 1998, to cancel all of these 4,759,580 shares by reducing the capital (for a par value of FRF 285,574,800), and by allocating the remainder to the "additional paid-in capital" item (FRF 4,501,327,443.40). In view, in particular, of shares acquired on the market between November 1 and December 31, 1998 and the exercising of former Compagnie de Suez purchase options, the Company held 467,056 in treasury stock as of December 31, 1998. The authorization vested in the Executive Board by the Ordinary and Extraordinary General Meeting of Shareholders on June 11, 1998 to trade in the Company's shares on the Stock Exchange expires at this General Meeting. It is proposed that a new authorization be today vested in the Executive Board to trade in the company's shares on the Stock Exchange with the broader perspective of active management of its equity in the light of its financing needs. In this context, it is specified that the new proposed limits are as follows:

- Maximum purchase price: EUR 250 (FRF 1,640)
- Minimum selling price: EUR 160 (FRF 1,050)

However, in the event of the options offered by Article 217-2 section 3 of the law relating to business corporations being exercised, such price is determined in accordance with the legal provisions in force.

- Maximum number of shares that may be held: 10% of share capital on the date of this decision.

Such authorization shall expire at the close of the General Meeting convened to deliberate on the accounts for the 1999 fiscal year, and within eighteen months at the latest.

Authority for the purpose of issuing bonds and debt securities

The Ordinary and Oxtraordinary General Meeting of Shareholders on June 11, 1998 authorized the company, for a period of five years, to issue bonds and debt securities of the company for a maximum nominal amount of FRF 10 billion, and to accompany such bonds with securities or marketable securities, in the form of warrants or otherwise, giving access to marketable securities which are representative of debts of the company, for a maximum nominal amount of FRF 5 billion. On the basis of such authorization, since your last meeting, your company has carried out two major transactions:

1 - within the scope of the public offer of exchange with regard to the capital of Société Générale de Belgique which took place in June and July 1998 and in order to remunerate the contribution of 25,396,358 Société Générale de Belgique shares, your company issued 25,396,358 new shares and 25,396,358 guaranteed value certificates. Such certificates, which guarantee a maximum value of FRF 180 per GVC, were recorded in off-balance sheet commitments for a total of approximately FRF 4.6 billion.

2 - in March 1999, your company issued options to be exchanged for AXA shares for an amount of EUR 787 million, i.e. approximately FRF 5.2 billion.

The authorization for five years vested in the Executive Board by the Ordinary and Extraordinary General Meeting of Shareholders on June 11, 1998 was used almost in full. It is therefore proposed that this authorization be renewed for larger amounts for another five-year period:

- Maximum limit for the issue of bonds and debt securities: EUR 5 billion (FRF 32.8 billion).
- Maximum limit for shares or marketable securities, in the form of warrants or otherwise, linked to the above-mentioned bonds and giving access to securities that are representative of debts of the Company: EUR 2.5 billion (FRF 16.4 billion).

2. Executive Board's Report to the Extraordinary General Shareholders' Meeting

In the extraordinary part of this Meeting, you are requested firstly to authorize an amendment of the by-laws (**tenth resolution**) with a view to enabling future meetings to use all voting methods permitted by law and that make use of advanced techniques, e.g., the counting of votes by means of electronic systems.

You are then requested to renew the authority vested in the Executive Board with regard to the issue of marketable securities, with corresponding cancellation of previous authorizations. Within this perspective, it is proposed that:

- **In the eleventh resolution,** you give the Executive Board authorization with a view to issuing, with the maintenance of shareholders' preferential subscription rights, shares, warrants and/or marketable securities which give access, either immediately or in the long-term, to shares (convertible bonds, shares or bonds with attached equity warrants, bonds which may be redeemed in shares, etc.) and to increasing the capital by capitalization of reserves. The nominal amount of the shares which could be issued in this way would be limited, excluding capitalization of reserves, to EUR 700 million (FRF 4.59 billion) and that of initial bond securities to EUR 5 billion (FRF 32.8 billion). The amounts of the issues carried out pursuant to the twelfth resolution would be offset against these amounts. The maximum nominal amount of an increase in capital carried out by capitalization of reserves would be limited to the overall amount of the sums which could be capitalized. The validity of this authority as set out by the eleventh resolution is twenty-six months.

- **In the twelfth resolution,** which includes the cancellation of the shareholders' preferential subscription rights, you enable the Executive Board to issue, on the French and/or international market, the same securities as those referred to under the eleventh resolution. Furthermore, this authority enables the Executive Board to issue securities whose purpose is to remunerate securities transferred to the Company in the context of a public offer of exchange where it is the offeror. Furthermore, such authority makes it possible to issue shares entitlement to which would result from marketable securities which would be issued, in agreement with your Executive Board, by direct or indirect subsidiaries of Suez Lyonnaise des Eaux. The nominal amount of the shares which could be issued in the context of the twelfth resolution would be limited, as in the case of the eleventh resolution, to EUR 700 million (FRF 4.59 billion) with that of initial bond securities being limited to EUR 5 billion (FRF 32.8 billion). The amounts of the issues carried out as part of the eleventh resolution would be offset against these amounts (and vice versa). The validity of this authority as set out by the twelfth resolution is he same as that set out by the eleventh resolution, i.e. twenty-six months.

The authorizations which are proposed to you will give your Executive Board great flexibility, where applicable, to carry out the issues that are best suited to the potential of the markets. Apart from the option of offering the Company's shareholders the opportunity to subscribe for new securities with attractive conditions, the Executive Board will, through launching issues without preferential subscription rights, be able to carry out transactions whose swiftness is a prerequisite of success while continuing to attract a larger public by launching issues on foreign financial markets.

In all cases where preferential subscription rights are maintained, aside from preferential subscription rights as of right, a preferential subscription right for excess shares enabling holders of old securities to subscribe for a greater number of securities than that to which they may subscribe by preferential right in proportion to their preferential subscription rights and in accordance with their requests may be established.

Where preferential subscription rights are eliminated, the Executive Board may grant priority of subscription, which does not enable negotiable securities to be set up, to the shareholders. Under the same authority, it is stipulated that the issue of shares in capital take place on the basis of the average of the opening listed prices of the old share on ten consecutive trading days selected from the last 20 days of trading prior to the issue, following adjustment of this average in the event of a difference in value dates; it is further stipulated that, in the event of an issue of equity warrants, the sum received by the Company upon subscription of warrants will be taken into consideration in this calculation.

The thirteenth resolution makes provision for authorizing your Executive Board to use previous authorizations relating to increases in capital, not reserved for named beneficiaries, at the time of a public offer of securities issued by the Company, until the next meeting called to deliberate on the Company's accounts.

The fourteenth resolution aims to authorize the Executive Board, for a duration of eighteen months, to reduce capital by canceling treasury stock held by the Company, pursuant to Article 217-2 of the Law of July 24, 1966; the Executive Board would have the power, in compliance with legal and regulatory provisions, to reduce capital by a maximum of 10% of its total amount.

The fifteenth resolution will allow the Executive Board, for a period of one year, and eliminating preferential subscription rights, to increase share capital by issuing new shares for a total nominal amount of EUR 15,000,000, reserving the subscription in such capital to Spring Multiple 99 SCA, a Luxembourg *société en commandite par actions* (partnership limited by shares). Such reserved increase in capital aims to encourage development of employee share ownership by granting foreign employees access to newly issued shares via this company in which they are to hold shares. Value creation and the ongoing concern for shareholder value creation in your Group, whose main resources are the employees of our Group, have led the Executive Board to decide to launch an operation aimed at encouraging share ownership by employees in order to:

- To make them full partners of your Group,
- To focus on value creation as a point where your interests and theirs meet,
- To enable them to side with your views in the choices made throughout the year,
- To make the primarily French concept of employee shareholders, which currently accounts for less than 1% of capital, an international concept.

It is in this spirit that employees should be able to subscribe, directly or indirectly, for Suez Lyonnaise des Eaux shares next July. Such subscription will be carried out either via a "traditional fund" or a "guaranteed fund" which would in addition enable an employee to increase his or her saving capacity to a large extent. Such operations will take place within the scope of the authorization given in the twentieth resolution of the Ordinary and Extraordinary General Meeting of Shareholders on June 11 1998, with the exception of the guaranteed fund aimed at foreign employees.

Since the offer is being made concurrently to around fifteen foreign countries, it was found during the development of the product that the diverse range of local legal constraints meant that subscribers were at a disadvantage if they were foreign employees. This raises the question as to what interest foreign employees would have in taking up the subscription offer made to them.

Therefore, at the recommendation of our advisers and with a view to retaining the benefits to which the Group's employees have a right, regardless of their nationality, the Executive Board has deemed it necessary to offer foreign employees subscription for Suez Lyonnaise des Eaux shares via the intermediary of the Company set up in Luxembourg for such purpose, Spring Multiple 99 SCA. This will allow them access to the issue under the same conditions as those offered to French employees.

Since the increases in capital authorized in the twentieth resolution of the Ordinary and Extraordinary General Meeting of Shareholders on June 11, 1998 were only open to subscriptions by employees made directly or via an employee investment fund, and not using the system put in place, we request that you authorize the Executive Board to issue shares for the benefit of Spring Multiple 99 SCA, whose shareholders will mainly be composed of foreign employees of the Group, according to the same conditions as those granted to employees in accordance with said twentieth resolution, referred to above: the issue price of the shares will be equal to the price which will be determined in accordance with this same resolution. The Executive Board will thus be able, for a period of one year, to increase capital, eliminating preferential subscription rights in favor of Spring Multiple 99 SCA, for a maximum nominal value of EUR 15,000,000 by issuing a maximum number of 1,500,000 new shares of a par value of EUR 10 each. The equality of the conditions of the share subscription offer was submitted to an independent expert, Mr. Jean Borgeix, appointed by the President of the Commercial Court of Paris on April 12, 1999, and his report has been made available to you.

In accordance with the provisions of Article 155-2 of the Decree of March 23, 1967, a supplementary report will be drawn up by the Executive Board upon application of the resolutions by which the meeting authorizes the issue of marketable securities with preferential subscription rights eliminated.

This report will set out the final conditions of the transaction and will show:

- the impact on the position of the shareholder of the proposed issue, particularly with regard to its share of shareholders' equity at closing of the previous fiscal year, given the stipulation that if this closing is more than six months prior to the contemplated transaction such impact will be assessed in the light of an interim financial position drawn up according to the same methods and following the same presentation as the last annual report;
- the theoretical impact on the current stock market value of the share, worked out on the basis of the average of the 20 days of trading prior to the transaction.

This information will be provided taking into account all of the securities issued that are liable to give access to the capital.

The sixteenth to the twenty-second resolutions aim to request your approval for internal restructuring operations, the objective of which is to simplify and improve the structure of the Suez Lyonnaise des Eaux Group by means of the merger absorption of three subsidiaries which are wholly owned: Auxilex, Société Financière d'Epargne and DBLE.

As all the shares of the three companies taken over are held by Suez Lyonnaise des Eaux, such mergers will be carried out pursuant to law under the simplified regime provided for in Article L378-1 of the law relating to business corporations. This will not give rise to any increase in the capital of Suez Lyonnaise des Eaux or exchange parity. From accounting and tax standpoints, the three operations will take retroactive effect as of January 1, 1999, with contributions being made on the basis of the net book values as they appear in the last balance sheets closed as of December 31, 1998.

The planned mergers and the reports of the appraisers of capital contributions, Messrs. Dominque Ledouble and Marcel Peronnet, contain comments relating to the assets contributed.

After taking into account the merger of wholly-owned subsidiaries with Auxilex and with Société Financière d'Epargne, such contributions are mainly made up of shareholdings and investments, as well as cash.

Among the main assets contributed are:

- Auxilex:

• Long-term investments for	FRF 577,578,463.39
• Current assets for	FRF 43,461,551.40

- Société Financière d'Epargne:

• Long-term investments for	FRF 524,163,241.00
• Current assets for	FRF 25,367,272.12

- DBLE:

• Long-term investments for	FRF 4,669,721.26
• Current assets for	FRF 31,094,225.72

The value of net assets contributed by Auxilex amounts to FRF 513,278,689.27, and is made up of contributed assets of FRF 621,040,014.79 and liabilities of FRF 107,761,325.52, taking into account the merger with Auxilex of a wholly-owned subsidiary, prior to this merger.

As Auxilex holds 915,954 Suez Lyonnaise des Eaux shares, Suez Lyonnaise des Eaux would reduce its capital by canceling 349,789 shares out of the 915,954 that would be contributed by Auxilex.

The merger surplus generated by the operation, i.e., FRF 301,575,838.89, minus the difference between the contribution value and the par value of the canceled shares, finally amounts to FRF 108,268,447.38, which will be recorded in an "additional paid-in capital" account.

The value of net assets contributed by Société Financière d'Epargne amounts to FRF 547,627,515.66, comprising contributed assets of FRF 549,530,513.11 and liabilities of FRF 1,902,997.45, after taking into account the merger with Société Financière d'Epargne of a wholly-owned subsidiary prior to this merger.

As Société Financière d'Epargne holds 1,090,631 Suez Lyonnaise des Eaux shares, Suez Lyonnaise des Eaux would reduce its capital by canceling all of the 1,090,631 shares that would be contributed to it by Société Financière d'Epargne.

The merger surplus generated by the operation amounts to FRF 39,826,968.66; the difference between the contribution value and the par value of the canceled shares, i.e., FRF 452,622,537.11, will be allocated in part to the total amount of the merger surplus and for the remainder to the "additional paid-in capital" item.

The value of net assets contributed by DBLE amounts to FRF 35,398,876.98, which breaks down as contributed assets of FRF 35,763,946.98 and liabilities of FRF 365,070.00.

The merger deficit generated by the operation, i.e. FRF 227,158,782.00, will be allocated to the income statement.

It is planned, moreover, for costs, taxes and fees incurred due to the merger operations, as well as the sums necessary for allocations to the special long-term capital gains reserve, to be offset against the "additional paid-in capital" item.

OBSERVATIONS OF THE SUPERVISORY BOARD ON THE EXECUTIVE BOARD'S REPORT AND THE ACCOUNTS FOR THE 1998 FISCAL YEAR.

At its Meeting on March 31, 1999, the Supervisory Board examined the report to be presented to the General Meeting by the Executive Board, as well as the accounts for the 1998 fiscal year, in the presence of the Statutory Auditors and with the participation of the Audit Committee.

These accounts had been prepared by the Executive Board, the Statutory Auditors having indicated that they would certify them without any qualification.

The Group share of net income amounted to EUR 1 billion (FRF 6.6 billion), up 64.3% from 1997, for revenue of EUR 31.4 (FRF 205.7 billion). This revenue, up 8% overall, has increased particularly in the core businesses (+17%), and more especially internationally (+65%).

The Group share of net income at EUR 0.76 billion (FRF 5 billion) is up 25.2%; it has increased by 50% in two years. The increase is particularly significant in the Energy sector in light of the increase in the capital of Société Générale de Belgique and new international developments in Tractebel.

The recorded growth is entirely in line with the objective declared at the time of the merger of doubling current net income per share by 2002.

Extraordinary income was recorded from the sale of Saint Gobain securities and the reduction of the holding in Fortis, partly counterbalanced by the creation of additional provisions to meet potential contingencies relating to emerging countries, restructuring provisions and exceptional amortization of goodwill.

The financial structure of the Group is solid with a non-financial sector net debt ratio of 59%; the rate of coverage of financial expenses by the gross operating income is 7.5.

Over the fiscal year the major sales of assets, combined with recurrent annual self-financing, enabled the Group to invest EUR 10.9 billion (FRF 71.5 billion), distributed between three large, broadly equivalent, areas: physical investments, acquisitions and the public offer of exchange with regard to Société Générale de Belgique.

Suez Lyonnaise des Eaux's parent company accounts show income of EUR 691 million, which justifies the proposal of a net dividend per share of EUR 2.70 (FRF 17.71).

The Supervisory Board was, at all times, able to perform its task of management control of the Group through the Executive Board. The Executive Board informed it in due course of any significant changes and enabled it to fulfil its purpose.

Special Statutory Auditors' Report on the proposals of the eleventh, twelfth, fourteenth, and fifteenth resolutions submitted for the approval of the Ordinary and Extraordinary General Meeting of Shareholders

To the Shareholders of Suez Lyonnaise des Eaux,

Acting in our capacity as the Statutory Auditors of your Company and in compliance with the tasks provided for by the Law of July 24, 1966, we hereby provide our report on the proposals of the eleventh, twelfth, fourteenth, and fifteenth resolutions submitted for the approval of the Ordinary and Extraordinary General Meeting of Shareholders with the aim of authorizing your Executive Board to carry out the following operations.

1. Issues of marketable securities

The operations contemplated are as follows:

- share capital increase by the issue, with maintenance of preferential subscription rights, of warrants and/or marketable securities which give access, immediately or in the long term, to Company shares, by limiting the amount of shares issued to EUR 700 million by subscription, conversion, exchange, redemption, presentation of a warrant or by any other means (eleventh resolution);
- share capital increase by the issue, with a waiver of preferential subscription rights, of shares, warrants and/or marketable securities which give access, immediately or in the long term, to Company shares (twelfth resolution);
- share capital increase with elimination of preferential subscription rights, for a maximum amount of EUR 15 million, in favor of Spring Multiple 99 SCA, a company organized and existing under Luxembourg law, in order to favor the share ownership of foreign employees (fifteenth resolution).

The delegations of powers that you are asked to give in the twelfth and fifteenth resolutions provide for the waiver of the preferential subscription rights relating to the shares to be issued. Your Executive Board seeks a delegation of powers from you in order to fix the terms and conditions of these operations.

We have examined the planned share capital increases and issues performing such procedures as we have deemed necessary in accordance with generally accepted professional standards.

Subject to a later examination of the conditions of the proposed operations, we have no comments to make on the methods of calculating the issue prices provided in the Executive Board's report.

As neither the amount of the issue and subscription prices nor the other terms and conditions of the issue have been fixed, we are not expressing our opinion on the final conditions under which the operations will be performed nor, consequently, on the proposal made to you to waive the preferential subscription right, the principle of which nevertheless falls within the logic of the operations submitted for your approval.

In accordance with Article 155-2 of the Decree of March 23, 1967, we shall draw up a supplementary report when your Executive Board decides to carry out the authorized operations.

2. Reduction in capital

The operation contemplated is the reduction of capital by canceling shares totaling a maximum of 10% of the capital of your Company (fourteenth resolution).

Your Executive Board seeks a delegation of powers from you in order to fix the terms and conditions of these operations.

We have analyzed the planned reduction in capital by cancellation of shares performing such procedures as we have deemed necessary in accordance with generally accepted professional standards.

As the terms and conditions of this reduction in capital have not been fixed, we are not expressing our opinion on the final conditions under which such operations might be performed.

In accordance with Article 215 of the Law of July 24, 1966 and Article 184 of the Decree of March 23, 1967, we shall draw up a supplementary report when your Executive Board decides to carry out the authorized operations.

Paris and Neuilly, April 16, 1999

The Statutory Auditors

Barbier Frinault & Autres
Arthur Andersen:
Christian Chochon

Mazars & Guérard:
Frédéric Allilaire

Allilaire.

REPORT OF THE APPRAISERS OF CAPITAL CONTRIBUTIONS IN ACCORDANCE WITH ARTICLES 193 AND 378-1 OF THE LAW OF JULY 24, 1966

To the Shareholders of Suez Lyonnaise des Eaux,

Pursuant to an order of February 15, 1999, the Presidents of the Commercial Courts of Nanterre and Paris appointed us as the appraisers of capital contributions in charge of assessing the value of contributions within the framework of the merger of DBLE, SFE and Auxilex into Suez Lyonnaise des Eaux.

We hereby present to you our report on these operations. Our report is organized as follows.

1. Presentation of the operation
2. Assessment of the value of contributions
3. Procedures performed
4. Conclusion

1. Presentation of the operation

The companies involved in the operation:

Suez Lyonnaise des Eaux (SLE) is a French *société anonyme* (joint-stock corporation) with capital of EUR 1,477,677,370 whose registered office is at 72, avenue de la Liberté, Nanterre 92000, France; it is registered with the Commercial and Companies Registry of Nanterre under the number 542 062 559.

DBLE is a French *société anonyme* (joint-stock corporation) with capital of FRF 6,000,000 whose registered office is at 72, avenue de la Liberté, Nanterre 92000, France; it is registered with the Commercial and Companies Registry of Nanterre under the number 338 512 353.

Société Financière d'Epargne (SFE) is a French *société par actions simplifiée* (simplified joint-stock corporation) with capital of FRF 190,000,000 whose registered office is at 4, place des Saussaies, Paris 75008, France; it is registered with the Commercial and Companies Registry of Paris under the number 341 970 416.

Auxilex is a French *société anonyme* (joint-stock corporation) with capital of FRF 209,000,000 whose registered office is at 4, place des Saussaies, Paris 75008, France; it is registered with the Commercial and Companies Registry of Paris under the number 712 010 867.

Conditions of the operation

SLE is considering absorbing DBLE, SFE and Auxilex through a simplified merger, as it should be noted that on the date of the merger agreement SLE holds all the shares of DBLE, SFE and Auxilex.

The net assets contributed amount to FRF 35,398,876.98 for DBLE, FRF 547,627,515.66 for SFE and FRF 513,278,689.27 for Auxilex; these contributions will not give rise to any issue of shares in the absorbing company.

The treatment applicable to the operations is the following:

- From a corporate law standpoint, the operations are considered as mergers/absorptions that are subject to the provisions of Article 378-1 of the Law of July 24, 1966.
- From a tax standpoint, the operations benefit from the preferential tax treatment provided for by Article 210-A of the French Tax Code, with respect to direct taxes; with respect to registration taxes, the operations are subject to the tax treatment under Article 816 of the French Tax Code; with respect to VAT, the absorbing company shall be subrogated in the rights and obligations of the absorbed companies.
- From accounting and tax standpoints, the operations shall be deemed to occur with retroactive effect as of January 1, 1999, and all the operations carried out with respect to assets and liabilities since that date shall benefit SLE.

Purpose of the operation

SLE is planning to restructure its internal organization. The absorptions planned for the purpose of streamlining and simplifying its structures will make it possible to consolidate the holding of investments and liquid assets.

2. Assessment of the value of contributions

DBLE, SFE and Auxilex are contributing the following assets and liabilities:

	DBLE	SFE	AUXILEX	TOTAL
Fixed assets	4,669,721.26	524,163,241.00	577,578,463.39	1,106,411 425
Current assets	31,094,225.72	25,367,272.11	43,461,551.40	99,923,049.23
Total assets	35,763,946.98	549,530.11	621,040,014.79	1,206,334,474.88
Provisions			16,568,895.00	16,568,895.00
Debts	365,070.00	1,902,997.45	91,192,430.52	93,460,497.97
Total liabilities	365,070.00	1,902,997.45	107,761,325.52	110,029,392.97
Net assets	**35,398,876.98**	**547,627,515.66**	**513,278,689.27**	**1,096,305,081.91**
Value of the shares on the SLE balance sheet	262,557,658.98	507,800,547.00	211,702,850.38	982,061,056.36
Merger surplus or deficit	(227,158,782.00)	39,826,968.66	301,575,838,89	

The contribution values correspond to the net book values as of December 31, 1998.

Merger surplus or deficit

The difference between the gross value of DBLE shares on SLE's balance sheet (FRF 262,557,658.98) and the value of contributions (FRF 35,398,876.98) corresponds to the overall merger deficit, which amounts to FRF 227,158,782.00. This amount will be entered on the income statement.

The difference between the value of contributions (FRF 547,627,515.66) and the value of the SFE shares on SLE's balance sheet (FRF 507,800,547.00) corresponds to the overall merger surplus, which amounts to FRF 39,826,968.66. This amount will be entered in the additional paid-in capital item.

The difference between the value of contributions (FRF 513,278,689.27) and the value of the Auxilex shares on SLE's balance sheet (FRF 211,702,850.38) corresponds to the overall merger surplus, which amounts to FRF 301,575,838.89. This amount will be entered in the additional paid-in capital item.

Reductions in capital

Pursuant to the Auxilex and SFE mergers, SLE will receive its own shares that will be canceled as follows:

	SFE	AUXILEX
Contribution value	524,163,241.00	216,252,045.82
Par value	(71,540,703.89)	(22,944,654.31)
Reduction in the additional paid-in capital	412,795,568.45	193,307,391.51

After the absorption of SFE, your company will become the owner of 1,090,631 of its own shares that will be canceled. This reduction in capital will be booked, beyond the par value, in the "additional paid-in capital" item.

For the Auxilex merger, SLE will receive 951,954 of its own shares, 349,789 of which will be canceled. Canceling these shares will give rise to a reduction in capital up to the par value; the surplus will be booked in the "additional paid-in capital" item.

3. Procedures performed

We have performed such procedures as we have deemed necessary in accordance with the professional standards laid down by the French National Institute of Statutory Auditors.

In particular:

- we have verified the ownership of all the shares of the capital of DBLE, SFE and Auxilex by SLE.
- we have reviewed the accounts of DBLE, SFE and Auxilex as of December 31, 1998.
- we have verified that the results of the interim period do not have a negative impact on the overall value of the contributions.

4. Conclusion

We have no comments to make on the overall value of the aforementioned contributions, which amount to a total of FRF 1,096,305,081.90

Paris, April 14, 1999

Dominique Ledouble

Marcel Péronnet

Statutory Auditors

Independent expert's report

On the terms and conditions of the increase in capital reserved for Spring Multiple 99 SCA for employees of foreign subsidiaries

Dear Shareholders,

Acting in my capacity as an independent expert appointed by an order of the Commercial Court of Nanterre on April 12, 1999, hereby present to you my report on the increase in capital reserved for Spring Multiple 99 SCA, a company organized and existing under Luxembourg Law, created upon the request of your Executive Board to offer foreign employees of your Group an employee savings plan under conditions that are comparable to those offered to French employees.

As presented by your Executive Board in its report, the purpose of this plan is to make it possible, through Spring Multiple 99 SCA, for foreign employees of your Group who wish to participate in the leveraged employee savings plan to take advantage of conditions to subscribe for new Suez Lyonnaise des Eaux "SLE" shares that are the same as those offered to employees of French companies as part of the group savings plan.

In accordance with the provisions governing group savings plans, French employees can subscribe, through an employee's investment fund, for SLE shares at a price that is 20% lower than the average share prices quoted on the stock exchange over the twenty consecutive days of trading prior to the Executive Board's decision to issue shares to French employees, pursuant to the twentieth resolution of the Extraordinary General Meeting of Shareholders on June 11, 1998.

The increase in capital reserved indirectly for employees of foreign subsidiaries of the SLE Group would enable them to subscribe for SLE shares under the following conditions:

• the increase in capital resulting from this subscription must not exceed a ceiling of 1,500,000 shares as decided by the Executive Board on March 29, 1999 and will be carried out, on one or more occasions, within a period of one year.

• the subscription price will be exactly the same as the price offered to French employees, i.e. with a 20% discount compared to the average share price quoted on the stock exchange over the twenty consecutive days of trading prior to the Executive Board's decision to issue shares to French employees.

The purpose of this report is to examine the conditions for the increase in capital reserved for Spring Multiple 99 SCA and it does not focus on the specific terms and conditions used to organize this company in order to reproduce, by using a single subscription price, an economic structure for the employees of foreign subsidiaries that is as similar as possible to the structure from which employees of French companies of the Group benefit.

Based on the various documents that were provided to me, an analysis of the operation that you are asked to approve leads me to confirm that the subscription price offered to the foreign employees of your Group through Spring Multiple 99 SCA is the same as the price also offered to French employees.

In order to ensure the same conditions for subscription, the increases in capital carried out for employees of French companies and employees of foreign subsidiaries will take place simultaneously.

It is thus your responsibility to evaluate the subscription conditions thereby offered to Spring Multiple 99 SCA and to approve or reject the resolution on this operation that is proposed by your Executive Board.

Paris, April 26, 1999

Jean Borjeix
Pinatton Finance

RESOLUTIONS

A) Deliberating as an Ordinary General Shareholders' Meeting

First Resolution - Approval of the operations and the accounts for the 1998 fiscal year

The General Meeting, deliberating in the form of an Ordinary General Meeting, having examined the reports of the Executive Board and the Statutory Auditors as well as the Observations of the Supervisory Board, approves the operations of the 1998 fiscal year as well as the accounts as of December 31, 1998 as they are presented to it.

Second Resolution - Appropriation of income and determination of the dividend amount

The General Meeting, deliberating in the form of an Ordinary General Meeting and noting that net income for the fiscal year amounts to EUR 691,151,531.51 (FRF 4,533,656,851.54) and retained earnings amount to EUR 4,647,387.49 (FRF 30,484,863.53), approves the appropriation of these sums, which represent a total of EUR 695,798,919.00 (FRF 4,564,141,715.07), as it is proposed by the Executive Board, namely:

	EUR	FRF
- Special long-term capital gains reserve	98,031,901.19	643,047,118.10
- Dividend payment to 147,767,737 actions	398,972,889.90	2 617,090,599.40
- *Special equalization tax*	128,015,521.25	839,726,772.70
- Retained earnings	70,778,606.66	464,277,224.87
	695,798,919.00	4,564,141,715.07

Consequently, the General Meeting sets the net dividend for the 1998 fiscal year at EUR 2.70 (FRF 17.7) per share, to which a tax credit of EUR 1.35 (FRF 8.85) will be added, giving total revenue per share of EUR 4.05 (FRF 26.56).

The dividend will be paid as of June 1, 1999 which is the cutting-off date.

It is specified that in the event that, at the time of such payment, the Company holds treasury stock, the sum corresponding to unpaid dividends for the amount of such shares would be included in retained earnings.

The Meeting takes note, in accordance with the law, of the sums distributed for the three previous fiscal years:

Fiscal Year	Number of shares upon which the dividend is paid		Sums distributed	Net dividend	Tax credit	Overall income
1995	58,045,706	EUR	101.7 millions	1.75	0.88	2.63
		FRF	667.5 millions	11.50	5.75	17.25
1996	59,315,239	EUR	108.5 millions	1.83	0.91	2.74
		FRF	711.7 millions	12.00	6.00	18.00
1997	126,235,772	EUR	288.6 millions	2.29	1.14	3.43
		FRF	1,893.5 millions	15.00	7.50	22.50

Third Resolution - Special Report of the Statutory Auditors

The General Meeting, deliberating in the form of an Ordinary General Meeting, having examined the special report of the Statutory Auditors on the agreements referred to under Articles 101 and 143 of the Law of July 24, 1966, approves the operations entered into or carried out during the fiscal year.

Fourth Resolution - Consolidated financial statements

The General Meeting, deliberating in the form of an Ordinary General Meeting, notes that the consolidated financial statements as of December 31, 1998 were presented to it and that the report of the Executive Board on Group management is included in the management report.

Fifth Resolution - Renewal of the term of office of a member of the Supervisory Board

The General Meeting, deliberating in the form of an Ordinary General Meeting, renews the term of office of Mr. Albert Frère as a member of the Supervisory Board, for one year.

Mr. Albert Frère's term of office will come to an end at the close of the annual Ordinary General Meeting which will deliberate on the accounts for the 1999 fiscal year.

Sixth Resolution - Appointment of a principal Statutory Auditor

The General Meeting, deliberating in the form of an Ordinary General Meeting, appoints as principal Statutory Auditor, for six fiscal years, Deloitte Touche Tohmatsu - Audit, a French *société anonyme* (joint-stock corporation) with capital of FRF 3,664,200, having its registered office at 185 avenue Charles de Gaulle, Neuilly-sur-Seine 92200, France, and registered with the Commercial and Companies Registry of Nanterre under the number 572 028 041 RCS Nanterre.

Deloitte Touche Tohmatsu - Audit's term of office will expire at the close of the Ordinary General Meeting which will deliberate on the accounts for the 2004 fiscal year.

Seventh Resolution - Appointment of a deputy Statutory Auditor

The General Meeting, deliberating in the form of an Ordinary General Meeting, appoints as deputy Statutory Auditor, for six fiscal years, Bureau d'Etudes Administratives Sociales et Comptables "BEAS", a French *SARL* (limited liability company) with capital of FRF 50,000, having its registered office at 7-9 villa Houssay, Neuilly-sur-Seine 92200, France, and registered with the Commercial and Companies Registry of Nanterre under the number 315 172 445 RCS Nanterre.

Bureau d'Etudes Administratives Sociales et Comptables "BEAS" will be the deputy to Deloitte Touche Tohmatsu - Audit and its term of office will expire at the same time as that of Deloitte Touche Tohmatsu - Audit.

Eighth Resolution - Authority to be vested in the Executive Board to trade in Company shares

The General Meeting, deliberating in the form of an Ordinary General Meeting and having examined the report of the Executive Board and the contents of the information memorandum approved by the *Commission des Operations de Bourse* (French Securities and Exchange Commission), authorizes the directorate, with the possibility of sub-delegation, to acquire shares of the company, under the conditions laid down by Article 217-2 of the Law of July 24, 1996 with a view:

- to their subsequent cancellation within the scope of a reduction in capital which would be agreed or authorized by the Extraordinary General Meeting,
- to them being retained and, where applicable, transferred, sold or exchanged within the scope of financial transactions, or asset and financial management of capital and equity.
- to them being allocated or transferred to employees or former employees of the Group, or to setting up stock option plans,
- to adjusting the market price of the Company's shares on the basis of the following terms:

- the maximum number of shares acquired may not exceed 10% of the share capital on the date of the decision herein and the accrued amount of acquisitions net of charges may not exceed the sum of EUR 3.6 billion,
- the maximum purchase price must not exceed EUR 250,
- the minimum selling price must not be less than EUR 160. However, in the event that the powers offered by section three of the above-mentioned Article 217-2 are used, the selling price will then be determined in accordance with the legislation in force.

The purchase of shares as well as their sale or transfer may be made by any means, on the market or by mutual agreement, including by using any financial instrument or by transactions involving options such as the purchasing and selling of put or call options. To this end, the Executive Board may, in particular, decide to allocate to shareholders, without payment, negotiable warrants which allow their holders, if they exercise them, at any time, or during periods defined by the Executive Board, to sell to the company a fixed number of shares for a price set by the Executive Board in accordance with the resolution herein. These transactions for the purchase, sale, transfer or issue of negotiable warrants may be carried out at any time, including at the time of a public offer.

In the event of an increase in capital by capitalization of reserves and the allocation of shares without payment, as well as in the event of either a stock split or consolidation, the prices indicated above will be adjusted arithmetically in the required proportion by the variation in the total number of shares determined by the operation.

Such authorization will be valid until the close of the General Meeting to deliberate on the accounts for the 1999 fiscal year and within eighteen months at the latest.

This resolution cancels and supersedes that passed by the Ordinary and Extraordinary General Meeting of Shareholders on June 11, 1998 in its ninth resolution for the amount of the authorization not used.

Ninth Resolution - Authority to be vested in the Executive Board for the purpose of issuing bonds and debt securities

The General Meeting, deliberating in the form of an Ordinary General Meeting, having examined the report of the Executive Board:

- Cancels the authority to issue ordinary bonds and debt securities given to the Executive Board by the Ordinary and Extraordinary General Meeting of Shareholders held on June 11, 1998;
- Authorizes the Executive Board, for a period of five years as from the date of this Meeting:

- to issue, on one or more occasions, at times that it will decide upon, on the French and/or the international market, one or several fixed- or variable-rate bond issues, whether perpetual or not, for a definite or an indefinite term, in euros, in foreign currencies, or in any other currency unit drawn up by reference to a group of currencies, for a maximum nominal amount of EUR 5 billion or the equivalent value of this sum in any other currency; and to generally issue, under the same conditions, any marketable securities that are representative of debts with regard to the Company, which may not exceed the sum of EUR 5 billion or the equivalent value of this sum as indicated above, it being specified that the accumulated amount of the above-mentioned issues of bonds and debt securities may not exceed the amount of EUR 5 billion or the equivalent value of this sum;
- to accompany the above-mentioned bonds with any securities or marketable securities, in the form of bonds or otherwise, giving access, by subscription or by any other manner, to debt securities of the Company, for a maximum nominal amount of EUR 2.5 billion or the equivalent value of this sum, with this amount being added to that set out above;

• Delegates full powers to the Executive Board in order to decide on such issues; to determine all of the terms and conditions of issue and redemption including in the form of exchange and allocation for payment of all assets and securities as well as of determination and payment of interest rates; the amount of the redemption premium, if one is provided for, will be added to the above amount of EUR 5 billion; to enter into any agreements to ensure their investment and successful conclusion; to make stock market redemptions with a view to partly redeeming the bonds; and, generally, to take all necessary measures and to do whatever is required.

B) Deliberating as an Extraordinary General Shareholders' Meeting

Tenth Resolution - Amendment of Article 34 of the by-laws relating to the voting method

The General Meeting, deliberating in the form of an Extraordinary General Meeting and having examined the report of the Executive Board, decides to amend the by-laws with a view to allowing the use of all voting methods at future General Meetings.

Consequently, the General Meeting decides to replace the third paragraph of Article 34 of the by-laws, with effect from the close of this Meeting, with the following wording:
"the votes of the shareholders present or represented by a duly authorized representative may be expressed by all means that comply with the laws and regulations in force."

Eleventh Resolution - Authority to be given to the Executive Board for the purpose of increasing the share capital, either by the issue, with maintenance of preferential subscription rights, of shares, warrants and/or marketable securities which give access, immediately or in the long term, to Company shares or by the capitalization of premiums, reserves, profits or suchlike

The General Meeting, deliberating in the form of an Extraordinary General Meeting, having examined the report of the Executive Board and the special report of the Statutory Auditors and in accordance with the provisions of the Law relating to business corporations, and in particular with Article 180:

1. Cancels the authorizations conferred on the Executive Board by the Ordinary and Extraordinary General Meeting of Shareholders held on June 11, 1998 with the purpose of increasing the share capital, partly through the issue, with maintenance of preferential subscription rights, of shares, warrants and/or marketable securities which give access, immediately or in the long term, to Company shares or by the capitalization of premiums, reserves, profits or suchlike,
2. Delegates to the Executive Board the powers required to carry out a share capital increase, on one or several occasions, in the proportion and at times that it shall determine:
   a) by issuing, in euros or in foreign currencies, or in any other currency unit established by reference to a group of currencies, shares, warrants and/or marketable securities giving immediate or long-term access, at any time or on a fixed date, to company shares by subscription, conversion, exchange, redemption, presentation of a warrant or by any other means,
   b) and/or by capitalizing premiums, reserves, profits or suchlike where such capitalization is possible pursuant to law and the by-laws and takes the form of an allocation of shares without payment or an increase in the par value of existing shares.

3. fixes the period of validity of this authority at twenty-six months as from this General Meeting;
4. decides to fix the limits of the amounts of authorized issues in the event of the Executive Board using its delegation of powers as follows:
   - in the event of a capital increase carried out in the context of the issues referred to in 2/a above:
   a) the maximum nominal amount of shares which may be issued in this way, either directly or upon presentation of securities, whether representative of debts or not, may not exceed the ceiling of EUR 700 million, or the equivalent value of this amount, to which will be added the overall nominal value of the shares that may be issued to maintain the rights of the holders of these securities in accordance with the law; it is stipulated that the nominal amount of the shares issued, whether directly or not, will be offset against this amount, pursuant to the twelfth resolution of this Meeting,
   b) the maximum nominal amount of the above-mentioned marketable securities that are representative of debts of the company which may be issued in this way may not exceed the ceiling of EUR 5 billion, or the equivalent value of this amount; it is stipulated that the nominal amount of the debt securities that will be issued will be offset against this amount, pursuant to the twelfth resolution of this Meeting;
   - in the event of the capitalization of premiums, reserves, profits or suchlike: the maximum nominal amount of capital increase which may be effected in this way may not exceed the overall amount of the sums that may be capitalized; it is stipulated that the amount of such capital increases will be added to the amount of the fixed ceiling mentioned above in "4/a";
5. in the event of the Executive Board using its delegation of powers, in the context of the issues referred to in "2/a" above:
   - decides that preference in these issue(s) will be given to shareholders who can subscribe by way of right;
   - nevertheless gives the Executive Board the power to grant shareholders the right to subscribe for excess shares to a higher number of marketable securities than that which they could subscribe to by way of right, in proportion to the preferential subscription rights that they have and, in any event, according to demand;
   - decides that if subscriptions by way of right, and where applicable, subscriptions for excess shares, have not accounted for the whole issue, the Executive Board may, under the conditions provided for by the Law and in the order that it shall decide upon, use any of the following powers:
     - to limit the capital increase to the amount of the subscriptions, provided that this reaches at least three-quarters of the agreed increase,
     - to freely distribute all or part of the securities issued but not subscribed,
     - to offer all or part of the securities issued but not subscribed for to the public on the French and/or international market;
   - decides that any issue of equity warrants that is likely to be made by the company may take place either by subscription offer, under the conditions set out above, or by the allocation of shares without payment to holders of old shares; in the event of the issue of warrants without payment, the Executive Board shall have the power to decide that the fractional shares allotment rights will not be negotiable and that the corresponding bonds will be sold, the sums resulting from the sale being allocated to those holding rights at the latest within 30 days of the registration date of the entire number of warrants allotted,
   - notes and decides, if need be, that this authority automatically entails, to the benefit of the holders of the securities issued, the express waiver by the shareholders of their preferential subscription rights to the securities to which the securities issued provide entitlement;
   - decides that the amount of the counterpart to which the company is entitled or may be entitled at a later date for each of the shares issued in the context of this authority will be at least equal to 80% of the average of the opening listed prices of the share on the Paris Stock Exchange monthly settlement market over ten consecutive days of trading selected from the last 20 days of trading prior to the start of the issue of shares and/or the securities providing entitlement thereto following adjustment, where applicable, of this average in the event of a difference between value dates; it is further stipulated that, in the event of an issue of company shares by way of subscription of warrants not attached to shares, the sum received by the company upon subscription of the warrants will be taken into consideration in this calculation;
6. decides that the Executive Board will have full powers to implement this authority, under the conditions set down by

law, for the particular purpose of:

• fixing capital increase and/or issue conditions,

• relating to any issues carried out in the context of the authority referred to in "2/a" above:

- deciding the amount to be issued, the issue price as well as the amount of the premium which may, where applicable, be requested at the time of the issue,
- setting the dates and terms and conditions of the issue, the type and form of securities to be set up, which can notably take the form either of perpetuals or not and for a fixed term or not, fixing the interest rates of the debt securities, their method of redemption, including via an exchange or allocation for payment of all assets or securities and their fixed or variable redemption price with or without a premium,
- determining the method of paying up for shares and/or securities issued,
- fixing, if applicable, the terms and conditions of exercising rights attached to securities issued or to be issued and, in particular, setting the date, which may even be retroactive, from which the new shares will bear rights of enjoyment, as well as any other terms and conditions relating to performing the issue,
- fixing the terms and conditions, where applicable, to redeem or exchange the securities issued or to be issued,
- providing for the power to possibly suspend the exercise of the rights attached to these securities for a period of a maximum of three months,
- fixing the terms and conditions by which, where applicable, the maintenance of the rights of the holders of the marketable securities giving access to company shares in the long-term will be carried out, in accordance with the laws and regulations,
- by its own initiative, offsetting the share capital increase expenses against the amount of the premiums relating to it and deducting from this amount the necessary sums to increase the legal reserve to one-tenth of the new capital figure, following each increase,

• relating to any capitalization of premiums, reserves, profits or suchlike:

- fixing the amount and the type of the sums to be capitalized, fixing the number of new shares to be issued or the amount by which the par value of existing shares which make up the share capital will be increased, setting the date, which may even be retroactive, from which the new shares will bear rights of enjoyment or at which the increase in the par value shall take effect,
- deciding, where applicable, as an exception to the provisions of Article 194 of the Law of July 24, 1966, that the fractional share rights shall not be negotiable and that the corresponding shares shall be sold, with the sums resulting from the sale being allocated to the holders of the rights at the latest 30 days after the registration date of the entire number of bonds allotted;

• in general, entering into any agreements, in particular to bring the contemplated issue to a successful conclusion, taking any measures and carrying out any formalities necessary for the issue and financing of securities issued under this authority as well as to the exercise of the rights that are attached thereto, recording the capital increase(s) carried out by using this authority and amending the by-laws correspondingly.

Twelfth Resolution - Authority to be given to the Executive Board for the purpose of increasing the share capital, either by the issue, with elimination of preferential subscription rights, of shares, warrants and/or marketable securities which give access, immediately or in the long term, to Company shares, including for the purpose of remunerating shares which are to be contributed within the scope of a public offer of exchange.

The General Meeting, deliberating in the form of an Extraordinary General Meeting, having examined the report of the Executive Board and the special report of the Statutory Auditors and in accordance with the provisions of the law relating to business corporations, and in particular with Article 180 as well as its Articles 193-1, 194-1 and 339-3:

1. Cancels the authorization granted to the Executive Board by the Ordinary and Extraordinary General Meeting of Shareholders held on June 11, 1998 for the purpose of increasing the share capital through the issue, with elimination of preferential subscription rights, of shares, warrants and/or marketable securities which give access, immediately or in the long term, to Company shares,
2. Delegates to the Executive Board the powers required to carry out a share capital increase, on one or more occasions, in the proportion and at times that it shall determine, on the French and/or international market by making public offers either in foreign currencies, euros or in any other

currency unit established by reference to a group of currencies, through the issue:

• by the Company of shares, warrants and/or marketable securities giving immediate or long-term access, at any time or on a fixed date, to Company shares whether by subscription, conversion, exchange, redemption, presentation of a bond or by any other means; it is stipulated that these securities may be issued for the purpose of remunerating stock that would be transferred to the Company in the context of a public offer of exchange relating to stock which meets the conditions laid down in Article 193-1 of the law relating to business corporations,

• and/or by one of the companies in which Suez Lyonnaise des Eaux holds, either directly or indirectly, over half of the capital, and with the agreement of such company:

- either of bonds with Suez Lyonnaise des Eaux equity warrants,
- or of any other marketable securities providing entitlement by conversion, exchange, redemption, presentation of a warrant or any other means to the allotment, at any time or on any date, of securities which, to this end, are or will be issued representing a share in the capital of Suez Lyonnaise des Eaux; it is stipulated that such marketable securities may take the form of shares with attached equity warrants, of bonds that are convertible into shares, of bonds redeemable in shares or any other form which would not be incompatible with the laws in force;

3. Fixes the validity of this authority at twenty-six months as from this General Meeting;
4. Decides to fix the limits of the amounts of authorized issues in the event of the Executive Board using its delegation of powers as follows:
   a) the maximum nominal amount of shares which may be issued in this way, either directly or upon presentation of securities, whether representative of debts or not, may not exceed the ceiling of EUR 700 million, or the equivalent value of this amount, to which will be added the overall nominal value of the shares that may be issued to maintain the rights of the holders of these securities in accordance with the law; it is stipulated that the nominal amount of the shares issued, whether directly or not, will be offset against this amount, pursuant to the eleventh resolution of this Meeting,
   b) the maximum nominal amount of marketable securities that are representative of the above-mentioned debts of the Company which may be issued in this way may not exceed the ceiling of EUR 5 billion, or the equivalent value of this amount; it is stipulated that the nominal amount of the debt securities that will be issued will be offset against this amount, pursuant to the thirteenth resolution of this meeting;
5. Decides to eliminate shareholders' preferential subscription rights with regard to securities that are subject to this resolution; these securities may be issued by the Company itself or by a company in which it holds, either directly or indirectly, over half of the capital, leaving the Executive Board the power, however, to give the shareholders, for a given period and according to the terms and conditions that it will set, and for all or part of the issue carried out, a subscription priority which does not result in the creation of negotiable rights;
6. Decides that if the subscriptions by shareholders and the general public have not accounted in full for an issue of marketable securities, the Executive Board may use, in the order that it shall determine, any of the following powers:
   - to limit the issue to the amount of subscriptions provided that this reaches at least three-quarters of the agreed issue;
   - to freely distribute all or part of the non-subscribed securities.
7. Notes and decides, if need be, that this authority automatically entails, to the benefit of the holders of the securities issued, the express waiver by the shareholders of their preferential subscription rights to the securities to which the securities issued provide entitlement;
8. Decides that the amount of the sum attributable or that may become attributable to the Company at a later date for each of the cash shares issued or to be issued in the context of this authority will be at least equal to the minimum value as stated by law, i.e. currently the average of the listed opening prices of the share on the Paris Stock Exchange monthly settlement market over ten consecutive days of trading selected from the last 20 days of trading prior to the start of the issue of shares and/or securities providing entitlement thereto following adjustment, where applicable, of this average in the event of a difference between value dates; it is further stipulated that, in the event of an issue of Company warrants not attached to shares or bonds, the sum received by the Company upon subscription of the warrants will be taken into consideration in this calculation;

9. Decides that the Executive Board will have full powers to implement this authority, under the conditions set down by law, for the particular purpose of:
   - fixing the conditions of the issue(s), in agreement with the appropriate bodies of the subsidiaries, if necessary,
   - deciding the amount to be issued, the issue price as well as the amount of the premium which may, where applicable, be requested at the time of the issue,
   - determining the dates and terms and conditions of the issue, the type and form of securities to be set up, which can notably take the form either of perpetuals or not and for a fixed term or not, fixing the interest rates of the debt securities, the method of redemption including via an exchange or allocation for payment of all assets or securities, and their fixed or variable redemption price with or without a premium,
   - determining the method of paying up shares and/or securities issued,
   - deciding that the balance of the issue which could not be subscribed shall be distributed at its discretion, either partly or fully, or that the amount of the issue shall be limited to the amount of subscriptions received; it is stipulated that the Executive Board may use, in the order that it shall deem necessary, all of the above powers or just one of them,
   - fixing, if necessary, the terms and conditions of exercising rights attached to securities issued or to be issued and, in particular, setting the date, which may even be retroactive, from which the new shares will bear rights of enjoyment, as well as any other terms and conditions relating to performing the issue,
   - fixing the terms and conditions, where applicable, of redemption or exchange of the securities issued or to be issued,
   - providing for the power to possibly suspend the exercise of the rights attached to these securities for a period of a maximum of three months,
   - more especially, in the event of the issue of securities for the purpose of remunerating securities transferred in the context of a public offer of exchange:
     - drawing up a list of securities transferred by exchange,
     - setting the issue conditions, the exchange parity as well as the amount of the equalization payment in cash to be paid,
     - determining the terms and conditions of the issue in the context of either a public offer of exchange, an alternative purchase or exchange offer or a main takeover bid or a public offer of exchange, accompanied by a takeover bid or a public offer of exchange in a secondary capacity,
   - by its own initiative, offsetting the share capital increase expenses against the amount of the premiums relating to it and deducting from this amount the necessary sums to increase the legal reserve to one-tenth of the new capital figure, following each increase,
   - in general, entering into any agreements, in particular to bring the contemplated issue to a successful conclusion, taking any measures and carrying out any formalities necessary to the issue and financing of securities issued under this authority as well as to the exercise of the rights that are attached thereto, recording the capital increase(s) carried out by using this authority and amending the by-laws correspondingly.

Thirteenth Resolution - authority to be given to the Executive Board for the purpose of using the authorizations to increase capital relating to Company securities at the time of a takeover bid or public offer of exchange

The General Meeting, deliberating in the form of an Extraordinary General Meeting and having examined the report of the Executive Board, decides that the various authorities given to the Executive Board by this meeting, relating to increases in capital not reserved for named beneficiaries, may under the legal conditions then in effect, be used, in full or in part, by such Executive Board, at the time of a takeover bid or public offer of exchange in relation to the marketable securities issued by the Company, for a period between the date of this meeting and that of the next meeting called to deliberate on the Company's accounts.

Fourteenth Resolution - Authority to be given to the Executive Board for the purpose of reducing capital by canceling shares

The General Meeting, deliberating in the form of an Extraordinary General Meeting, having examined the report of the Executive Board and the special report of the Statutory Auditors:

- authorizes the Executive Board, for a period of eighteen months and pursuant to Article 217-2 of the Law of July 24, 1966, to reduce the capital, on one or more occasions, by canceling treasury stock held by the company, by a maximum of ten percent of the Company's capital within a period of twenty-four months,
- grants the Executive Board full powers to:

- carry out this (these) reduction(s) in capital,
- decide on the final amount, fix the terms and conditions and record that it has been carried out,
- offset the difference between the book value of the canceled shares and their nominal value against all reserves and premium items,
- amend the by-laws correspondingly and generally do whatever is necessary.

All the above in compliance with the legal provisions applicable at the time this authorization is used.

Fifteenth Resolution - Authorizations to increase the share capital, with the elimination of preferential subscription rights, in favor of Spring Multiple 99 SCA

The General Meeting, deliberating in the form of an Extraordinary General Meeting, having examined the report of the Executive Board, the special report of the Statutory Auditors as well as the report of the independent expert appointed by the President of the Commercial Court of Nanterre:

- authorizes the Executive Board to increase the share capital, on one or more occasions, for a period of one year as of the date of this Meeting, by a nominal maximum value of EUR 15,000,000 by issuing a maximum number of 1,500,000 new shares with a nominal value of EUR 10 each;
- decides to eliminate the preferential subscription rights of shareholders and to reserve subscription of all shares to be issued to Spring Multiple 99 SCA, a Luxembourg *société en commandite par actions* (partnership limited by shares), with capital of EUR 31,000, having its registered office at 3, avenue Pasteur, L-2311 Luxembourg, which is in the process of being registered;
- decides that the issue price of the new shares will be identical to that set by the Executive Board, which will set the terms and conditions of the next issue of shares reserved for the Group's employees pursuant to the twentieth resolution of the Ordinary and Extraordinary General Meeting of the Shareholders on June 11, 1998, with the price set by the Executive Board being equal to 80% of the average of the opening listed prices on the Paris Stock Exchange monthly settlement market over the last 20 days of trading prior to the date of its decision;
- grants full powers to the Executive Board, in particular to:
  - set the date(s) and the terms and conditions of the share issues that will be made in accordance with the authorization herein; in particular, to set the number of new shares to be issued, their date of enjoyment, which may even be retroactive, and the issue price in compliance with the above-defined rules,
  - if need be, decide that the amount of the increase in capital or of each increase in capital will be limited to the amount of each subscription received,
  - enter into any agreements, and carry out, either directly or indirectly, any operations and formalities,
  - make amendments to the by-laws relating to increases in the share capital,
  - offset the charges of the increases in share capital against the amount of the premiums pertaining to such increases, and deduct from such amount the sums necessary to increase the legal reserve to a tenth of the amount of the new capital after it has been increased,
  - and, in general, do what is required.

Sixteenth Resolution - Approval of the agreement on the merger-absorption of Auxilex by Suez Lyonnaise des Eaux

The General Meeting, deliberating in the form of an Extraordinary General Meeting, having examined the report of the Executive Board, the report of the Appraisers of Capital contributions, as well as the merger agreement which was signed with Auxilex, a French société anonyme (joint-stock corporation) with capital of FRF 209,000,000 having its registered office at: 4, place des Saussaies, 75008 Paris, France, registered with the Commercial and Companies Registry of Paris under the number 712 010 867 RCS Paris, under the terms of which such company will, pursuant to the merger, contribute all its assets to Suez Lyonnaise des Eaux:

- Approves the merger agreement and decides on the merger with Auxilex by the absorption of such company;
- Approves the contributions made by Auxilex pursuant to the merger and the valuation of such contributions that has been made;
- And, noting that the various conditions precedent to which this merger was subject have been fulfilled, decides that the merger of Suez Lyonnaise des Eaux with Auxilex is final and binding;
- Consequently notes that Auxilex is wound up without undergoing liquidation as of the day hereof.

Seventeenth Resolution - Determination and calculation of the merger surplus resulting from the adoption by this meeting of the sixteenth resolution

The General Meeting, deliberating in the form of an Extraordinary General Meeting, having examined the report of the Executive Board:

- Notes that as the merger is to be carried out under the regime of Article l 378-1 of the Law of July 24, 1966 relating to business corporations, the adoption of the preceding resolution does not entail any new shares being issued;
- Decides, in light of the fact that Suez Lyonnaise des Eaux, owing to the completion of this merger, holds 915,954 in treasury stock with a par value of EUR 10 each previously held by Auxilex, to cancel 349,789 of such shares by reducing the capital by an amount of EUR 3,497,890;
- Decides that the difference between the contribution value of the canceled shares, equal to FRF 216,252,045.82 and the nominal value of 349,789 shares canceled, i.e., EUR 3,497,890 (FRF 22,944,654.31) will be offset against the merger surplus for a sum of FRF 193,307,391.51;
- Notes that the merger surplus, in an amount of FRF 301,575,838.89, represented by the difference between the net value of the assets contributed (i.e., FRF 513,278,689.27) and the book value of the 100% shareholding in Auxilex in the accounts of Suez Lyonnaise des Eaux (i.e., FRF 211,702,850.38), less the difference (i.e., FRF 193,307,391.51) between the contribution value (i.e. FRF 216,252,045.82) and the nominal value of the canceled shares (i.e., EUR 3,497,890, equivalent to FRF 22,944,654.31), amounting to a sum of FRF 108,268,447.38, will be recorded in an "additional paid-in capital" item;
- Specially approves the provisions of the merger agreement with Auxilex relating to the allocation of the merger premium;
- Authorizes the Executive Board:
  - To offset against such merger premium all charges, duties, taxes and fees resulting from the merger operations;
  - To deduct from such premium the sums necessary for the special long-term capital gains reserve in accordance with the regulations in force;
- And authorizes the Ordinary General Meeting of shareholders to allocate such premium for all uses other than capitalization;
- Decides, as a consequence of the reduction in capital referred to in the current resolution, to change Article 6 of the by-laws relating to the share capital which henceforth will read as follows: "the share capital is set at EUR 1,474,179,480. It is divided into 147,417,948 shares of a par value of EUR 10 each, all of the same class."

Eighteenth Resolution - Approval of the agreement on the merger-absorption of Société Financière d'Epargne by Suez Lyonnaise des Eaux.

The General Meeting, deliberating in the form of an Extraordinary General Meeting, having examined the report of the Executive Board, the report of the Appraisers of Capital contributions as well as the merger agreement which was signed with Société Financière d'Epargne, a French *société par actions simplifiée* (simplified joint-stock company), with capital of FRF 190,000,000, having its registered office at: 4, place des Saussaies, 75008 Paris, France, and registered with the Commercial and Companies Registry of Paris under the number 341 970 416 RCS Paris, pursuant to which such company will, in respect of the merger, contribute all its assets to Suez Lyonnaise des Eaux:

- Approves the merger agreement and decides on the merger with Société Financière d'Epargne by the absorption of such company;
- Approves the contributions made within the scope of the merger by Société Financière d'Epargne and the valuation of such contributions that was made;
- And, noting that the various conditions precedent to which this merger was subject are fulfilled, decides that the merger of Suez Lyonnaise des Eaux with Société Financière d'Epargne is final and binding;
- Consequently notes that Société Financière d'Epargne is wound up without undergoing liquidation as of the date hereof.

Nineteenth Resolution - determination and allocation of the merger surplus resulting from the adoption by this General Meeting of the eighteenth resolution

The General Meeting, deliberating in the form of an Extraordinary General Meeting and having examined the report of the Executive Board:

- Notes that since the merger is to be carried out under the regime of Article l 378-1 of the Law of July 24, 1966 relating to business corporations, the adoption of the preceding resolution does not entail any new shares being issued;
- Decides, in light of the fact that Suez Lyonnaise des Eaux holds, owing to the completion of this merger, 1,090,631 treasury stock with a par value of EUR 10 each previously held by Société Financière d'Epargne, to cancel all of such shares by

reducing the capital by an amount of EUR 10,906,310;

- Decides that the difference between the contribution value of the canceled shares, equal to FRF 524,163,241.00 and the nominal value of the 1,090,631 canceled shares (FRF 71,540,703.89) will be offset against the full amount of the merger surplus and for the remainder to the "additional paid-in capital" item.
- Notes that:
- The merger surplus, represented by the difference between the net value of the assets contributed (i.e., FRF 547,627,515.66) and the book value of the 100% shareholding in Société Financière d'Epargne in the accounts of Suez Lyonnaise des Eaux (i.e., FRF 507,800,547.00) amounts to FRF 39,826,968.66;
- The difference between the contribution value (i.e., FRF 524,163,241.00) and the nominal value of the canceled shares (i.e., EUR 10,906,310, equivalent to FRF 71,540,703.89), which amounts to a sum of FRF 452,622,537.11 will be offset in part against the full amount of the merger surplus, and the balance (i.e., FRF 412,795,568.45) will be allocated to the "additional paid-in capital" item;
- Decides, as a consequence of the reduction in capital referred to in the current resolution, to amend Article 6 of the by-laws relating to the share capital which henceforth will read as follows: "the share capital is set at EUR 1,463,273,170. It is divided into 146,327,317 shares of a par value of EUR 10 each, of the same class."

Twentieth Resolution - Approval of the agreement on the merger-absorption of DBLE by Suez Lyonnaise des Eaux

The General Meeting, deliberating in the form of an Extraordinary General Meeting, having examined the report of the Executive Board, the report of the Appraisers of Capital contributions as well as the merger agreement which was signed with DBLE, a French *société anonyme* (joint-stock corporation) with capital of FRF 6,000,000, having its registered office at: 72, avenue de la Liberté, 92000 Nanterre, France, registered with the Commercial and Companies Registry of Nanterre under the number 338 512 353 RCS Nanterre under the terms of which such company will, pursuant to the merger, contribute all its assets to Suez Lyonnaise des Eaux:

- Approves the merger agreement and decides on the merger with DBLE by the absorption of such company;
- Approves the contributions made within the scope of the merger by DBLE and the valuation of them that was made;
- And, noting that the various conditions precedent to which this merger was subject are fulfilled, decides that the merger of Suez Lyonnaise des Eaux with DBLE is final and binding;
- Consequently notes that DBLE is wound up without undergoing liquidation as of the date hereof.

Twenty-first Resolution - Determination and allocation of the merger deficit resulting from the adoption by this meeting of the twentieth resolution

The General Meeting, deliberating in the form of an Extraordinary General Meeting and having examined the report of the Executive Board:

- Notes that since the merger is to be carried out under the regime of Article L 378-1 of the Law of July 24, 1966 relating to business corporations, the adoption of the preceding resolution does not entail any new shares being issued;
- Notes that the merger deficit, represented by the difference between the net value of the assets contributed (i.e., FRF 35,398,876.98) and the book value of the 100% shareholding in DBLE in the accounts of Suez Lyonnaise des Eaux (i.e., FRF 262,557,658.98) amounts to FRF 227,158,782.00, and decides to allocate this sum to the income statement;
- Specially approves the provisions of the merger agreement with DBLE relating to the allocation of the merger deficit.

Twenty-second Resolution - Allocations to the "additional paid-in capital" item

The General Meeting, deliberating in the form of an Extraordinary General Meeting, given the adoption of the resolutions relating to the Auxilex, Société Financière d'Epargne and DBLE merger-absorptions, authorizes the Executive Board:

- To offset against the "additional paid-in capital" item, if applicable, all charges, duties, tax and fees resulting from the merger operations;
- To draw the sums necessary for allocation to the special long-term capital gains reserve, in accordance with the tax regulations in force from the "additional paid-in capital" item.

Twenty-third Resolution - Powers to enforce the Meeting's decisions and for formalities

The General Meeting, deliberating in the form of an Extraordinary General Meeting, gives full powers to the bearer of an original, a copy or an excerpt of the minutes of this meeting in order to carry out any necessary filings and formalities.

Exhibit E2 to Application of United Water Florida, Inc. for Transfer of Majority Organizational Control of its Corporate Grandparent, United Water Resources, Inc. to Lyonnaise American Holding, Inc.

Lyonnaise American Holding, Inc.

(a wholly-owned subsidiary of Suez Lyonnaise des Eaux)

Consolidated Financial Statements

December 31, 1998 and 1997

Mazars & Guerard

Mazars & Guérard, LLP

CERTIFIED PUBLIC ACCOUNTANTS

INDEPENDENT AUDITOR'S REPORT

March 30, 1999

TO THE BOARD OF DIRECTORS OF
LYONNAISE AMERICAN HOLDING, INC.

In our opinion, based upon our audits and the report of other auditors, the accompanying consolidated balance sheets and the related consolidated statements of income and retained earnings and of cash flows present fairly, in all material respects, the financial position of Lyonnaise American Holding, Inc. and its subsidiaries (the "Company") at December 31, 1998 and 1997, and the results of operations and their cash flows for the years then ended in conformity with generally accepted accounting principles. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of United Water Services LLC and its subsidiaries, a consolidated investee, which comprises aggregate assets of $81.9 million and $58.3 million or 28% and 20% of the Company at December 31, 1998 and 1997 and incurred losses of $8.7 million and $5.2 million for the years then ended. In addition, we did not audit the investments in unconsolidated subsidiaries which amounted to $197.3 million and $182.7 million or 68% and 62% of the Company's aggregate assets at December 31, 1998 and 1997. Those statements were audited by other auditors whose report thereon has been furnished to us and our opinion, insofar as it relates to the amount included for United Water Services LLC and its subsidiaries, and the investments in unconsolidated subsidiaries is based solely on the reports of the other auditors.

We conducted our audits in accordance with generally accepted auditing standards which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the report of other auditors provide a reasonable basis for the opinion expressed above.

Mazars & Guerard, LLP

52 Vanderbilt Avenue New York, NY 10017
E-mail: info@mazarsusa.com
Telephone (212) 953-2570 • Telefax (212) 953-2575 • (212) 973-0661

Lyonnaise American Holding, Inc.
(a wholly-owned subsidiary of Suez Lyonnaise des Eaux)
Consolidated Balance Sheet

(thousands of dollars, except share amounts)	December 31, 1998	December 31, 1997
Assets		
Current assets:		
Cash and cash equivalents	$ 5,652	$ 1,237
Equity securities portfolio	-	45,000
Accounts receivable, net	24,026	12,388
Other current assets	2,080	1,408
Total current assets	31,758	60,033
Equity investments in unconsolidated affiliates, net of unamortized discount of $790 in 1998 and $1,071 in 1997	197,290	182,730
Goodwill, net	42,687	42,758
Costs and estimated earnings in excess of billings	7,962	-
Other investments	4,941	5,305
Property and equipment, net	2,969	899
Deferred income taxes	2,623	1,780
Other non-current assets	880	1,692
Total assets	$ 291,110	$ 295,197
Liabilities and Shareholder's Equity		
Current liabilities:		
Notes payable to banks	$ 16,700	$ 9,350
Current portion of long-term debt	1,400	-
Accounts payable	1,885	2,763
Accounts payable to affiliates	1,088	3,030
Income taxes	-	471
Other accrued expenses	10,713	3,037
Total current liabilities	31,786	18,651
Long-term debt	5,600	-
Deferred income taxes	8,857	7,286
Deferred gain on sale of affiliate	888	1,125
Minority interest	27,505	27,477
Commitments and contingencies (Note 8)		
Shareholder's equity		
Preferred stock (10,000 shares authorized; none issued)	-	-
Common stock (3,000 shares authorized; 2,248 shares issued & outstanding)	2	2
Additional paid in capital	208,204	208,204
Retained earnings	10,168	33,908
Accumulated other comprehensive income	(1,900)	(1,456)
Total shareholder's equity	216,474	240,658
Total liabilities and shareholder's equity	$ 291,110	$ 295,197

The accompanying notes are an integral part of these consolidated financial statements.

Lyonnaise American Holding, Inc.
(a wholly-owned subsidiary of Suez Lyonnaise des Eaux)
Consolidated Statement of Net Income

(thousands of dollars)	Year ended December 31, 1998	1997
Revenues	$ 67,450	$ 28,706
Cost of services	60,581	27,523
Gross profit	6,869	1,183
General and administrative expenses	19,196	10,540
Loss from operations	(12,327)	(9,357)
Other income and (expenses):		
Equity in earnings of affiliates	15,169	12,117
Preference dividends, net of amortization of discount	1,893	2,168
Income from equity securities portfolio	1,024	2,691
Gain on sales of subsidiaries	117	10,015
Goodwill amortization	(1,397)	(666)
Net interest income (expense) and other	(206)	738
Total other income	16,600	27,063
Income before income taxes	4,273	17,706
Income tax (benefit) expense	(819)	635
Net income before minority interest	5,092	17,071
Minority interest in losses of subsidiaries	5,168	2,722
Net income	$ 10,260	$ 19,793

The accompanying notes are an integral part of these consolidated financial statements.

Lyonnaise American Holding, Inc.
(a wholly-owned subsidiary of Suez Lyonnaise des Eaux)
Consolidated Statement of Cash Flows

(thousands of dollars)	Year ended December 31, 1998	Year ended December 31, 1997
Cash Flows from Operating Activities		
Net income	$ 10,260	$ 19,793
Adjustments to reconcile net income to cash provided by operating activities		
Depreciation and amortization	754	854
Goodwill amortization	1,397	443
Minority interest in losses of consolidated subsidiaries	(5,168)	(2,722)
Equity in earnings of affiliates higher than dividends received	(5,183)	(2,408)
Costs and estimated earnings in excess of billings	(7,962)	-
Changes in assets and liabilities:		
Accounts receivable	(11,919)	(2,748)
Accounts payable and other accrued expenses	5,077	1,498
Deferral of gain on sale of subsidiary	(118)	1,125
Other assets and liabilities	(1,500)	(1,882)
Cash provided by (used in) operating activities	(14,362)	13,953
Cash Flows from Investing Activities		
Acquisition of United Water Services Inc.	-	(23,185)
Acquisition of United Metering Inc.	-	(6,223)
Beginning cash balance of newly consolidated subsidiaries	-	2,004
Distributions from WREP	720	-
Basis of divested subsidiaries	-	34,477
Reinvestment of United Water Resources dividends	(9,986)	(9,242)
Other investments	(507)	(5,305)
Collection of notes receivable from minority interests	-	10,000
Capital expenditures	(2,370)	(416)
Withdrawals from equity securities portfolio	45,000	20,000
Cash provided by investing activities	32,857	22,110
Cash Flows from Financing Activities		
Equity contributions received from minority owners	5,570	10,755
Cash dividends paid	(34,000)	(55,395)
Net change in short term borrowings	14,350	9,150
Cash used in financing activities	(14,080)	(35,490)
Increase in cash and cash equivalents	4,415	573
Cash and cash equivalents at beginning of year	1,237	664
Cash and cash equivalents at end of year	$ 5,652	$ 1,237
Supplemental Disclosure:		
Cash paid during the year for interest	$ 928	$ 178
Cash paid during the year for income taxes	$ -	$ 1,133

The accompanying notes are an integral part of these consolidated financial statements.

Lyonnaise American Holding, Inc.
(a wholly-owned subsidiary of Suez Lyonnaise des Eaux)
Consolidated Statement of Changes in Shareholder's Equity

(thousands of dollars)	Common Stock	Preferred Stock	Additional Paid-In Capital	Retained Earnings	Other Comprehensive Income	Total
Balance at December 31, 1996	$ 1	$ 85,637	$ 115,540	$ 69,497	$ (2,684)	$ 267,991
Comprehensive income						
Net income				19,793		19,793
Foreign currency translation adjustment					1,228	1,228
Comprehensive income						21,021
Stock dividends			7,487	(7,487)		-
Cash dividends				(47,895)		(47,895)
Sale of subsidiary adjustment			(459)			(459)
Conversion of preferred stock to common	1	(85,637)	85,636			-
Balance at December 31, 1997	$ 2	$ -	$ 208,204	$ 33,908	$ (1,456)	$ 240,658
Comprehensive income						
Net income				10,260		10,260
Foreign currency translation adjustment					(444)	(444)
Comprehensive income						9,816
Cash dividends				(34,000)		(34,000)
Balance at December 31, 1998	$ 2	$ -	$ 208,204	$ 10,168	$ (1,900)	$ 216,474

The accompanying notes are an integral part of these consolidated financial statements.

1. Operations and Summary of Significant Accounting Policies

These consolidated financial statements include the accounts of Lyonnaise American Holding, Inc. (LAH, or the Company), a Delaware corporation that is a wholly-owned subsidiary of Suez Lyonnaise des Eaux, a French société anonyme, and the following subsidiaries in which LAH has more than a 50% direct or indirect ownership interest:

- United Water Services LLC, a limited liability company in which LAH and United Water Resources Inc. (United Water Resources) each own a 50% common membership interest. United Water Services was formed by LAH and United Water Resources as a partnership in 1994 and was converted to a limited liability company in 1997. United Water Services and its subsidiaries are involved in the business of providing operations, maintenance and management services for municipally-owned water and wastewater facilities in the United States of America.
- United Water Services Mexico LLC (UWS Mexico), a limited liability company in which LAH owns a 79.5% common membership interest and United Water Resources owns the remaining 20.5% interest. UWS Mexico was formed in connection with a North American reorganization in July 1997 for the purpose of providing operations, maintenance and management services for government-owned water and wastewater facilities in Mexico.
- United Water Services Canada LP and UWS Canada GP Inc. (collectively, UWS Canada), a Canadian limited partnership and its US corporate general partner in which LAH owns a 66.7% interest and United Water Resources owns the remaining 33.3% interest. These entities were also formed in connection with the North American reorganization in July 1997, for the purpose of providing operations, maintenance and management services for government-owned water and wastewater facilities in Canada.

LAH owns as its other principal assets the following investments:

- Approximately 29.5% of the outstanding common stock, and 98.1% of the outstanding convertible preference stock, of United Water Resources, a US water and wastewater services company whose stock is traded on the New York Stock Exchange.
- 49% of the outstanding stock of Tecnologia y Servicios de Agua, S.A. de C. V. (TECSA), a Mexican company that provides water-related services to a portion of Mexico City, Mexico.
- An approximate 48% investment by United Water Services as the Operating Partner in the White River Environmental Partnership (WREP), an Indiana partnership that provides wastewater services to the City of Indianapolis.
- A 50% investment by UWS Mexico in Aguas, Servicios e Inversiones de México, S. de R.L. de C.V. (ASIM), a Mexican joint venture formed to pursue opportunities to provide operations, maintenance and management services to municipally-owned water and wastewater facilities in Mexico.
- An approximate $3.3 million investment in the AIG-GE Capital Latin American Infrastructure Fund L.P. (the AIG-GE Capital Fund), a limited partnership fund that seeks long term capital appreciation through equity, quasi-equity and convertible debt investments in infrastructure projects and infrastructure related industries in Latin America and the Caribbean.

The Company accounts for its investments in United Water Resources, TECSA, WREP and ASIM under the equity method of accounting. The investment in the AIG-GE Capital Fund is accounted for under the cost method of accounting.

In July 1997, LAH and United Water Resources completed a reorganization of their joint North-American non-regulated water and wastewater operations. Prior to this reorganization, United Water Services Inc., formerly known as JMM Operational Services, Inc., was owned equally by United Water Services and by Montgomery Watson, Inc. (Montgomery Watson), a California-based engineering services company. The reorganization involved: (i) the purchase by United Water Services of the remaining 50% of United Water Services Inc. from Montgomery Watson; (ii) the sale to United Water Services by LAH of LAH White River Corporation, a wholly-owned subsidiary of LAH that owned a 5% interest in WREP; and (iii) the formation of UWS Mexico and UWS Canada to pursue non-regulated delegated water and wastewater services opportunities in those countries. Montgomery Watson owns a 10% convertible preferred membership interest in United Water Services. If the convertible preferred membership interest is not converted to a common membership interest before July 14, 2002, it will be redeemed with interest by United Water Services. The aggregate net payment made by United Water Services in connection with the purchase of the remaining 50% of United Water Services Inc. was $23.2 million, while the aggregate net cash payment made by LAH itself in connection with the entire North American restructuring was approximately $15.2 million. The following is a summary of this acquisition:

(thousands of dollars)		
Fair value of assets acquired	$	30,000
Cash paid for the capital stock		(23,185)
Preferred Membership Interest issued	$	6,815

The above transactions resulted in the recording of approximately $43.3 million of goodwill, including $1.8 million relating to United Water Services' purchase from LAH of LAH White River Corporation. Goodwill is being amortized over estimated lives that range from 10 to 40 years.

From the formation of UWS Mexico and UWS Canada in July 1997 until December 1998, Montgomery Watson owned a 10% interest in each. In December 1998, Montgomery Watson sold its 10% interest in each to LAH and United Water Resources. LAH purchased (i) 9.5% of Montgomery Watson's 10% ownership in UWS Mexico, increasing LAH's ownership from 70% to 79.5%, and (ii) 6.7% of Montgomery Watson's 10% ownership in UWS Canada, increasing LAH's ownership from 60% to 66.7%. United Water Resources purchased Montgomery Watson's remaining interests.

In December 1997, United Water Services purchased United Metering Inc., a company involved in the installation of water meters, from United Water Resources for its book value of $6.2 million.

In July 1997, LAH sold its 80% investment in Aqua-Chem, Inc. (Aqua-Chem), and as a result the Company's consolidated financial statements no longer include the accounts of Aqua-Chem. For periods prior to the sale of Aqua-Chem, the Company's investment in Aqua-Chem is accounted for using the equity method of accounting.

Description of Business

LAH is primarily a holding company. However, through its affiliates LAH provides (i) full facility operations and maintenance services for water and wastewater treatment and related facilities ("Contract Operations"), (ii) meter installation services, (iii) construction management and (iv) training and advisory services ("Operational Assistance"), all to municipal and other governmental entities and industrial clients in the United States, Mexico and Canada.

Basis of Presentation

Certain amounts in the 1997 financial statements and notes have been reclassified to conform to the 1998 presentation.

Use of Estimates
The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from these estimates.

Revenue Recognition
The Company derived approximately 83% and 90% of 1998 and 1997 revenues, respectively, from Contract Operations services and the remainder from Operational Assistance, construction management, meter installation and other services, generally with level monthly fees that are subject to adjustment for variances in plant operating conditions, maintenance requirements and inflation indices.

Subsidiaries engaged in long-term Contract Operations services record revenues and estimated profits under the percentage-of-completion method of accounting. The estimated profits under each agreement are reviewed and revised periodically, with adjustments being recognized on a cumulative basis in the period in which any revisions are made. Costs and estimated earnings in excess of billings are included in cost of services in the consolidated statement of income and retained earnings.

Revenues are recognized on the remaining short-term Contract Operations and Operational Assistance contracts as services are rendered to clients in accordance with contract terms. Provisions for anticipated losses on all contracts are made when losses become apparent.

As a result of United Water Services' Contract Operations accounted for under the percentage-of-completion method of accounting, future results may be affected by the significant estimates used by management. In addition, under one of those contracts, results under the percentage-of-completion method of accounting are largely dependent on future natural gas prices. Although a contract is in place to purchase gas at a fixed rate through the end of 2000, should future gas prices fluctuate dramatically, actual results could differ from management estimates. United Water Services attempts to mitigate these risks by monitoring gas trends closely and pursuing future supply contracts.

Property and Equipment
Property and equipment, which consists primarily of furniture and equipment, are recorded at cost. Depreciation is computed using the straight-line method over estimated lives ranging from 5 to 10 years. Amortization of leasehold improvements is computed using the straight-line method over the shorter of the lives of the improvements or the lease term.

Goodwill
Goodwill represents the difference between the purchase price and the book value of net assets acquired and is amortized on a straight line basis over a period of 10 to 40 years. Based on the evaluation of the realizability of goodwill and the basis of expected future cash flows, the Company believes no impairment exists.

Income Taxes
Deferred income taxes are provided for temporary differences between the financial reporting basis and the tax basis of the Company's assets and liabilities. The major temporary difference relates to the basis of the Company's investments in unconsolidated affiliates.

Translation of Foreign Currencies
The functional currency for TECSA is the Mexican peso, while the U.S. dollar has been determined to be the appropriate functional currency for UWS' international operations. The investment in TECSA is translated at the exchange rate prevailing at the balance sheet date, and the Company's equity in the earnings of TECSA is translated at the average exchange rate in effect during the year. Translation adjustments are accumulated as a component of stockholder's equity. Changes in foreign currency translation accounts were as follows:

(thousands of dollars)	1998	1997
Balance, beginning of year	$ (1,456)	$ (2,684)
Translation adjustments	(444)	(205)
Sale of investment in Aqua-Chem, Inc.	-	1,433
Balance, end of year	$ (1,900)	$ (1,456)

Fair Value of Financial Instruments
The fair value of cash, short-term investments, notes receivable and trade accounts receivable and payable approximates their carrying amounts in the accompanying consolidated balance sheet.

Cash and Cash Equivalents
For purposes of the Statement of Cash Flows, the Company considers all highly liquid investments with an initial maturity of three months or less to be cash equivalents.

2. Accounts Receivable

A summary of accounts receivable is as follows:

	December 31,	
(thousands of dollars)	1998	1997
Contract receivables, including unbilled amounts and retainage	$ 20,959	$ 10,672
Affiliates and other	3,055	1,694
Employee advances and other	37	47
Allowance for doubtful accounts	(25)	(25)
Total accounts receivable, net	$ 24,026	$ 12,388

3. Divestment of Subsidiary

In July 1997, LAH sold its 80% investment in Aqua-Chem, Inc., a diversified manufacturing company, and received $40 million of cash and shares of two series of redeemable, cumulative preferred stock of the purchaser (the "Series A Preferred Stock" and "Series B Preferred Stock "). In June 1998, Aqua-Chem redeemed 60% of its Series A Preferred Stock, and paid LAH (i) $2.4 million and (ii) the accrued but unpaid dividends on all of the shares of Series A Preferred Stock. The remaining unredeemed shares of Series A Preferred Stock are to be repaid in two equal installments in August 2000 and August 2001. Preferred dividends on the remaining Series A Preferred Stock are payable quarterly until redemption. The Series B Preferred Stock matures in July 2004, but permits earlier redemption in certain circumstances. The redemption amount of the Series B Preferred Stock is contingent upon the achievement of certain levels of economic performance by Aqua-Chem subsequent to the date of the sale. In addition, certain provisions allow Aqua-Chem, Inc. to reduce the redemption amount and accumulated dividends otherwise payable to LAH for certain liabilities that are subsequently paid by the purchaser but were not recorded on the books of Aqua-Chem at the date of the sale. The two series of Preferred Stock have been recorded in Other Investments at their estimated fair market value, net of the expected offsets for potential unrecorded liabilities.

4. Investment in Unconsolidated Affiliates

The investment in unconsolidated affiliates, net of unamortized discount, consisted of the following at December 31, 1998 and 1997:

	December 31,	
(thousands of dollars)	1998	1997
United Water Resources Inc.:		
Common stock	$ 160,190	$ 142,806
5% Series A Convertible Preference Stock	30,336	34,588
White River Environmental Partnership (WREP)	3,848	3,161
Tecnologia y Servicios de Agua, S.A. de C. V. (TECSA)	2,817	2,175
Aguas, Servicios e Inversiones de Mexico (ASIM)	99	-
	$ 197,290	$ 182,730

Summarized information regarding the unconsolidated affiliates (excluding ASIM, which has no operations) at December 31, 1998 is as follows:

(thousands of dollars)	United Water Resources	WREP	TECSA
Assets	$ 1,769,122	$ 19,413	$ 10,651
Liabilities	1,221,738	11,468	3,105
Equity (common and preferred)	547,384	7,945	7,546
Revenue	$ 356,210	$ 38,517	$ 17,954
Net income	$ 43,929	$ 2,942	$ 1,536

5. Issuance of Preferred Stock and Investment in Hedged Utility Stock Portfolio

During the second quarter of 1996, LAH invested $65 million in a portfolio consisting of US utility common stocks, and at the same time entered into a two year SWAP Agreement that essentially provided a hedge against changes in the value of that portfolio of utility stocks ($65 million of original notional value). The SWAP Agreement required LAH to pay the counter-party the dividends paid on the securities in the notional portfolio, in exchange for which LAH received quarterly payments on the then outstanding notional value at a rate based on the 90 day London Interbank Borrowing Rate (LIBOR). That rate was reset each quarter. In addition, the SWAP Agreement required LAH to pay the counter-party (or the counter-party to pay LAH) any increase (or decrease) in the value of the notional portfolio at maturity or at such earlier date(s) should LAH exercise its limited option to terminate the SWAP Agreement and withdraw funds from the portfolio, in whole or in part. prior to maturity. LAH exercised this withdrawal right twice in 1997, withdrawing a total of $20 million from the portfolio. In June 1998, LAH liquidated the remainder of the Equity Securities Portfolio when the SWAP Agreement expired, receiving the remaining $45 million balance of its original investment. LAH paid a $34 million cash dividend to Suez Lyonnaise des Eaux, and, after repaying short term debt outstanding, invested the remaining balance of the cash proceeds received in short term time deposits.

6. Property and Equipment

A summary of property and equipment is as follows:

(thousands of dollars)	December 31, 1998	December 31, 1997
Furniture and equipment	$ 4,323	$ 1,922
Leasehold improvements	239	99
	4,562	2,021
Less accumulated depreciation and amortization	(1,593)	(1,122)
	$ 2,969	$ 899

7. Income Taxes

Income tax expense (benefit) consists of the following:

(thousands of dollars)		Year Ended December 31, 1998	Year Ended December 31, 1997
Current:	Federal	$ (2,252)	$ 882
	State	(213)	(139)
	Total current	(2,465)	743
Deferred:	Federal	1,612	(104)
	State	34	(4)
	Total deferred	1,646	(108)
Total income tax expense		$ (819)	$ 635

The following table reconciles the statutory tax rates to the actual effective income tax rates for 1998 and 1997, which were (19.2%) and 3.6%, respectively:

(thousands of dollars)

	1998	1997
Statutory tax rate	35%	35%
Pretax income	$ 4,273	$ 17,706
Federal tax expense at statutory rates on pretax income	1,496	6,197
Minority interest in losses of subsidiaries	1,809	953
Effect of dividend received deduction on investment in United Water Resources	(3,346)	(3,187)
Tax gain lower than book gain on sale of Aqua-Chem, primarily due to the use of previously unrecognized prior years' net operating losses	(822)	(3,369)
State income taxes (benefit), net of federal benefit	(119)	(96)
Other	163	137
Income tax (benefit) expense	$ (819)	$ 635

Deferred income taxes reflect the tax effect of temporary differences between the amount of assets and liabilities for financial reporting purposes and for income tax purposes. The tax effects of each type of temporary difference that gives rise to a significant portion of the deferred tax assets and liabilities are as follows:

(thousands of dollars)	December 31, 1998	December 31, 1997
Net operating losses carryforward	$ 1,374	$ 589
Employee related accrued expenses	330	353
Other accrued expenses	738	738
Foreign tax credits	113	113
Valuation allowance for foreign tax credits	(74)	(74)
Book depreciation in excess of tax depreciation	36	46
Other	106	15
Deferred tax assets	2,623	1,780
Basis of investment in unconsolidated affiliates	(8,154)	(6,729)
Deferred mobilization costs	(416)	(270)
Partnership income	(287)	(287)
Deferred tax liabilities	(8,857)	(7,286)
Net deferred tax liability	$ (6,234)	$ (5,506)

8. Commitments and Contingencies

LAH has executed a subscription agreement to purchase a $10 million interest in a limited partnership formed to make Latin American investments. Through December 31, 1998, $3.3 million of this commitment had been funded.

United Water Services has various operating leases relating to equipment, automobiles and office and other space. At December 31, 1998, United Water Services had $55.9 million and $1.7 million of performance and bid bonds outstanding, respectively. United Water Services is generally responsible for returning the equipment used to operate the facilities, as well as any inventory obtained at the commencement of each contract.

United Water Services is involved in various litigation and other disputes routine to the nature of its business. After recording appropriate accruals, management believes no significant additional liability will result upon ultimate disposition of such matters.

9. Debt

At December 31, 1998, the Company and United Water Services had uncommitted credit facilities with banks for $50,000,000 and $105,000,000, respectively. At December 31, 1998, $16,700,000 had been borrowed by United Water Services under the facilities at a weighted average interest rate of 7.3%, and $7,186,000 of the facilities were utilized to support letters of credit for several projects and for a loan to WREP.

In June 1998, United Water Services entered into a $7,000,000 intermediate term financing with a bank. The loan is a five-year, unsecured loan at a fixed rate of 6.44% with constant annual payments of $1,4000,000.

10. Related Party Transactions

United Water Services provides various services to WREP, including management and human resources services. Employees of United Water Services operate the WREP projects, and WREP reimburses United Water Services for the costs of such services. Amounts due from WREP affiliates at December 31, 1998 and 1997 were $1,788,662 and $664,750, respectively.

Montgomery Watson periodically provides professional engineering services to United Water Services, and United Water Services serves as a subcontractor to Montgomery Watson in conjunction with various contracts.

United Water Resources and Suez Lyonnaise des Eaux also provide various services to LAH and certain of its affiliates, including management, human resource, engineering, accounting and corporate secretary and legal services. In addition, LAH and United Water Services rent office space from United Water Resources for its corporate headquarters. At December 31, 1998 and 1997, a combined $1,081,000 and $2,601,000, respectively, was owed to the affiliated companies. United Water Services also serves as a subcontractor to United Water Resources on a Contract Operations contract. Receivables due from United Water Resources of $1,624,000 and $1,284,000 at December 31, 1998 and 1997, respectively, and from Suez Lyonnaise des Eaux of $499,000 at December 31, 1998, are included in accounts receivable in the Consolidated Balance Sheet.

11. Defined Benefit Pension Plan

In February 1998, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 132. "Employers' Disclosures about Pensions and Other Postretirement Benefits." This statement addresses disclosure only. It does not address measurement or recognition. United Water Services adopted SFAS No. 132 in 1998.

Prior to August 1997, qualifying employees of the United Water Services were participants in a defined benefit pension plan offered by Montgomery Watson. Annual contributions made to Montgomery Watson relating to employees of the Company were charged to expense and amounted to $160,000 for the first 7 months of 1997. In August 1997, the Company established a trusteed, non-contributory, defined benefit pension plan ("UWS Pension Plan") initially funded by $1,381,484 spun-off from the Montgomery Watson plan. Benefits under this plan are based upon years of service and the employee's compensation during employment. United Water Services' policy is to fund the UWS Pension Plan at amounts equal to or greater than the minimum funding requirements of the Employee Retirement Income Security Act of 1974.

The components of net periodic pension expense were as follows:

(thousands of dollars)	Year Ended Dec. 31, 1998	Last 5 Months of 1997
Current year service cost	$ 575	$ 172
Interest cost	122	44
Return on plan assets	(141)	(53)
Amortization of unrecognized net loss	8	
Net periodic pension expense	$ 564	$ 163

The status of the funded plan was as follows:

(thousands of dollars)	1998	1997
Change in benefit obligation		
Benefit obligation at beginning of year	$ 1,461	$ 1,411
Service cost	575	172
Interest cost	122	44
Actuarial loss	320	64
Benefits paid	(23)	(230)
Benefit obligation at end of year	$ 2,455	$ 1,461
Change in plan assets		
Fair value of plan assets at beginning of year	$ 1,184	$ 1,355
Actual return on plan assets	306	59
Employer contributions	597	-
Benefits paid	(23)	(230)
Fair value of plan assets at end of year	$ 2,064	$ 1,184
Funded status	(391)	(277)
Unrecognized net actuarial loss	206	58
Prepaid/(accrued) benefit cost	$ (185)	$ (219)

The major actuarial assumptions used in the foregoing calculations were as follows:

	1998	1997
Assumed discount rate	7.125%	7.375-7.5%
Assumed compensation increase	4%	4%
Expected long-term rate of return on plan assets	10%	9.5%

The net periodic pension expense charged to WREP for employees of United Water Services who operate the WREP facilities totaled $300,559 in 1998 and $81,251 in 1997.

Supplemental Benefit Plan
United Water Services maintains a defined contribution savings plan. This plan permits employees to make voluntary contributions to the plan, and United Water Services contributes additional amounts as defined by the plan agreement. United Water Services' expense related to its contributions to the defined contribution plan amounted to $214,698 and $49,204 in 1998 and 1997, respectively.

Exhibit E3 to Application of United Water Florida, Inc. for Transfer of Majority Organizational Control of its Corporate Grandparent, United Water Resources, Inc. to Lyonnaise American Holding, Inc.

United Water

Setting the pace

1998 Annual Report

About United Water

United Water Resources (NYSE:UWR) is a holding company primarily engaged in water-related businesses. As the nation's second-largest investor-owned water services company, United Water provides water and wastewater services through its regulated utilities and non-regulated contract operations to over 7.5 million people in more than 400 communities in 19 states. The company also has investments in water services in Canada, Mexico and the United Kingdom. In addition, the company owns and manages real estate investments through a wholly-owned subsidiary. United Water has been listed on the New York Stock Exchange since 1889 and has paid cash dividends on its common stock continuously since 1886.

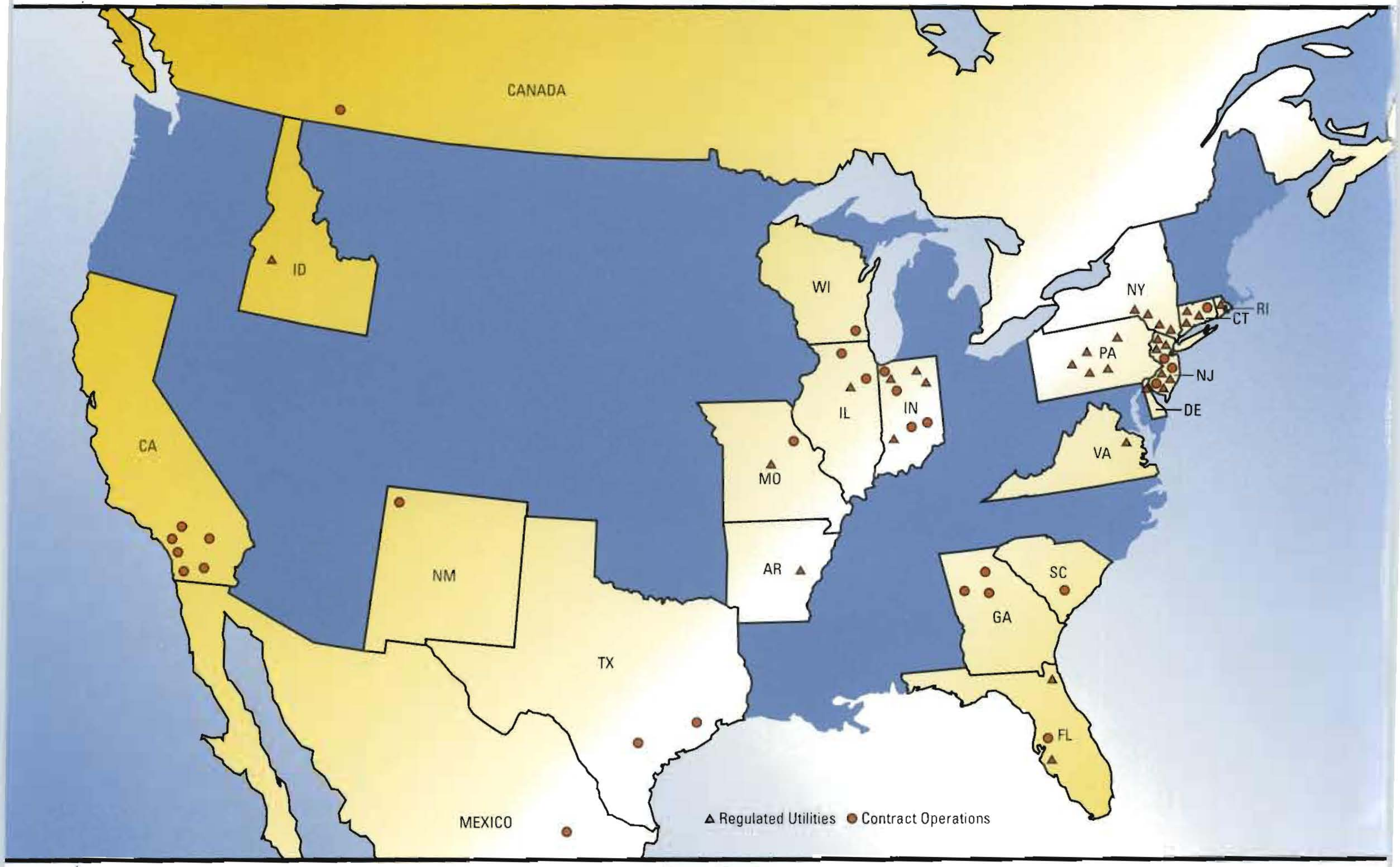
Contents

Financial Highlights

(THOUSANDS EXCEPT PER SHARE DATA)	1998	1997	1996
Operating revenues	$ 356,210	$ 351,409	$ 332,045
Net income (loss) applicable to common stock			
Continuing operations	$ 43,929	$ 29,331	$ 38,407
Discontinued operations	—		(4,397)
Total	43,929	29,331	34,010
Net income (loss) per common share			
Continuing operations	$ 1.19	$ .83	$ 1.14
Discontinued operations	—	—	(.13)
Total	1.19	.83	1.01
Average shares outstanding	37,028	35,492	33,707
Net income (loss) per common share-assuming dilution			
Continuing operations	$ 1.17	$ .83	$ 1.12
Discontinued operations	—	—	(.12)
Total	1.17	.83	1.00
Average shares outstanding	39,192	37,838	36,218
Dividends per common share	$ .93	$ .92	$ .92
Equity per common share	12.05	11.53	11.33

We are the leader in contract operations: the fastest growing segment of the water services industry.

United Water
At A Glance



United Water now serves over 7.5 million people in more than 400 communities in 19 states.

Regulated Utilities

Regulated utilities are United Water's core business. The company began in 1869 as a regional utility supplying water to communities in northern New Jersey. Over the years, United Water expanded its operations to include water and wastewater utilities around the country. Today United Water operates more than 30 utilities in 13 states. The company also has partial ownership in Northumbrian Water Group, a major investor-owned water and wastewater services company that serves approximately four million people in the United Kingdom.

ARKANSAS
Pine Bluff

CONNECTICUT
New Milford
Newtown
Woodbury

DELAWARE
Wilmington

FLORIDA
Jacksonville
Sarasota

IDAHO
Boise

ILLINOIS
Lincoln

INDIANA
Mooresville
Warsaw
West Lafayette
Winchester

MISSOURI
Jefferson City

NEW JERSEY
Bergen County
Hamilton
Hudson County
Lambertville
Mt. Arlington
Plainsboro
Toms River
Vernon
West Milford

NEW YORK
New Rochelle
Nichols
Owego
Rockland County

PENNSYLVANIA
Bethel Township
Bloomsburg
Dallas
Harrisburg
Mechanicsburg

RHODE ISLAND
Wakefield

VIRGINIA
Warsaw

Contract Operations

United Water and its United Water Services affiliate, which is owned on a 50/50 basis with Suez Lyonnaise des Eaux, manage water and wastewater systems under private contracts with communities in 12 states across the country. Services range from partial to full operation of all water-related activities. These activities include operating treatment plants, distribution and collection systems and maintaining reservoirs and watersheds, as well as managing customer service, billing and collections. United Water also has investments in companies that provide water-related services to cities and government entities in Canada and Mexico.

CALIFORNIA
Avalon
Banning
Burbank
El Segundo
San Diego
Western Riverside

CONNECTICUT
Killingly

FLORIDA
Pinellas County

GEORGIA
Atlanta
Big Canoe
Fulton County

ILLINOIS
Freeport
Pekin

INDIANA
Indianapolis
Boone County
Cumberland
Gary

MISSOURI
Stoutsville

NEW JERSEY
Hoboken
Jersey City
Manalapan
Wall Township

NEW MEXICO
Farmington

SOUTH CAROLINA
Lexington

TEXAS
Houston
San Antonio

WISCONSIN
Milwaukee

CANADA
Banff, Alberta

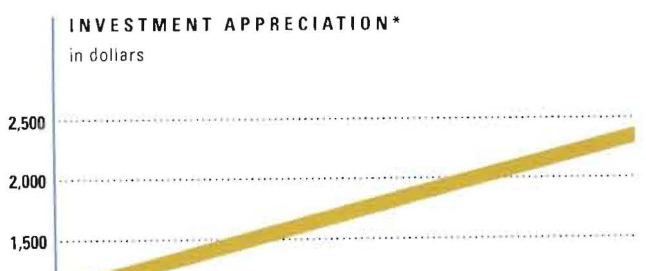
MEXICO
Mexico City

Dear fellow shareholders

Led by the continued strong performance of our utility investments, United Water achieved significant improvement in shareholder value in 1998:

- United Water's stock price rose 22 percent during the year, and has increased at a compound growth rate of 26 percent since year-end 1995, the first full year of operations following our 1994 acquisition of General Waterworks.
- United Water attained the second-highest earnings in our 129-year history in 1998. This marked the third consecutive year that the company increased earnings per share from continuing operations and before non-recurring items.
- And including dividends, we achieved a total return of 28.7 percent for the year. This follows a return to shareholders of 32.9 percent in 1997 and 37.9 percent in 1996.

The board of directors demonstrated its confidence in United Water's performance and prospects for continued growth by increasing the company's quarterly cash dividend paid on its common stock by 4.3 percent, from 23 cents to 24 cents.



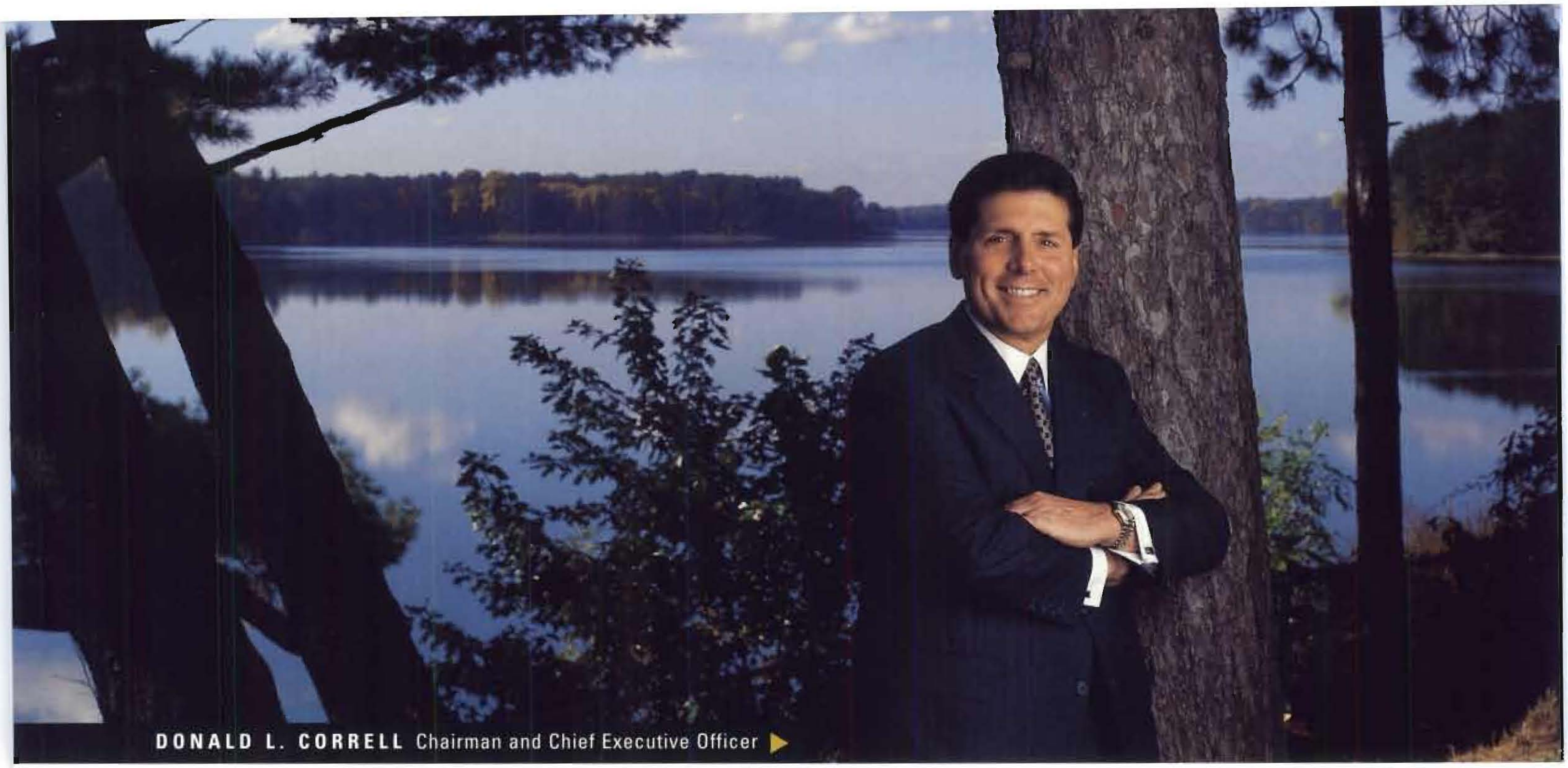
*$1,000 invested in 1995 grew to $2,414 in 1998.

Win Four Largest Contracts, Continue Strategy

Along with improved financial results, United Water through our affiliates attained leadership in the U.S. water services industry by winning all four of the major contract operations awarded by municipalities during the year. The four contracts are in Atlanta, Milwaukee, Gary, and the southern San Antonio area.

These new agreements continued the series of accomplishments achieved over recent years through steady and aggressive implementation of our corporate growth strategy.

We outlined our progress in advancing the strategy in our recent annual reports. In 1995 we started "building on our core water services business," as the foundation for expansion. This led to the "forging of a competitive team" that aggressively



marketed the company's strengths. In 1997 we "positioned" ourselves "for maximum growth" by strengthening and unifying our contract operations capability. By 1998, the progress we made in the previous three years culminated in United Water's achieving leadership and "setting the pace" for contract operations — the fastest growing segment in our industry.

Together with our affiliates we now operate three of the nation's largest municipal water systems (Atlanta, Houston and Jersey City) and three of the country's biggest municipal wastewater operations (Milwaukee, Gary, Indianapolis) under private contract.

United Water's corporate strategy and strengths are driving our successes. Our strategy aims to capitalize on the company's leading position in contract operations and the relationships with our strategic alliances, as well as to extend our utility service territories. Our plan also is designed to enhance the operations of our utilities through improved efficiencies, productivity and customer service.

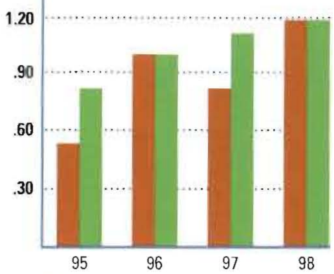
The major underlying strengths propelling our successes include our size as the nation's second-largest investor-owned water services company and our long track record of accomplishments. In addition, our leadership in contract operations gives us an edge in this highly competitive business.

Our utilities contribute to United Water's financial stability through steady, reliable and growing earnings. The company's market capitalization of approximately $800 million reinforces our financial foundation. Another strength is United Water's record of paying cash dividends on our common stock on a steady, reliable basis for 112 years.

Century of Leadership

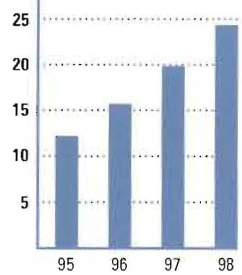
United Water's leadership in the water industry stretches back more than a century. The company pioneered the development of advanced water treatment systems and the construction of large reservoirs in northern New Jersey and southern New York State. We built our first reservoirs nearly a hundred years

EARNINGS PER SHARE
in dollars
12 months ended December 31



■ Earnings per share
■ Earnings per share from continuing operations and before non-recurring items

STOCK PRICE*
in dollars



*at December 31

ago and demonstrated a vision and concern for water quality rare for the time by protecting the watershed. We launched new initiatives throughout the 20th century. These included introducing automatic meter reading, constructing a state-of-the-art ozone water treatment facility, and partnering with a state agency to build a major regional water supply project.

Our leadership in contract operations dates back to the early 1990s with our aggressive marketing and business development program. In 1994 we created a national model through the country's first water services public-private partnership with Hoboken, New Jersey. Two years later we formed what was at the time the largest public-private partnership in the industry with Jersey City, New Jersey.

Across the nation, United Water has forged public-private partnerships that significantly improve municipal systems while saving the cities many millions of dollars. In 1998 United Water and the cities of Jersey City and Gary won awards for the benefits achieved through public-private partnerships. The U.S. Conference of Mayors recognized the operations in both cities, and the Jersey City partnership also won the annual Project Recognition Award from the National Council for Public-Private Partnerships.

Setting the Pace

United Water's advancements in technology and management of municipal systems reflect the company's historic role as a leader in the U.S. water services industry. With our 1998 achievements in contract operations, United Water is setting the pace in meeting the water and wastewater needs of cities across the country.

The leading role we achieved in 1998 was not accomplished overnight. Decades of successes by our utilities, and more recently our business development staff, contract operations affiliates, and strategic alliances, all have helped United Water become a front-runner.

The teamwork and pooling of our vast expertise and resources has enabled us to steadily expand our utility and contract operations. With the continued support of our employees and partners, and you, our shareholders, United Water will continue its commitment to long-term growth and increased shareholder value.

Donald L. Correll
Chairman and Chief Executive Officer
March 12, 1999

Setting the pace

By winning all the major new contract operations awarded by municipalities in 1998, United Water Resources and its affiliates are setting the pace in the U.S. water services industry. The company leads the nation in managing contract operations—the fastest-growing segment of the water services industry—and in meeting the current and future water and wastewater needs of cities across the country.

United Water gained—and retains—this leadership position by building on the strengths and track records of its utility and contract operations and by advancing the company's broad-based growth strategy. The strategy focuses on expansion through contract operations and acquisitions, as well as through joint programs with affiliates and strategic alliances.

United Water operates

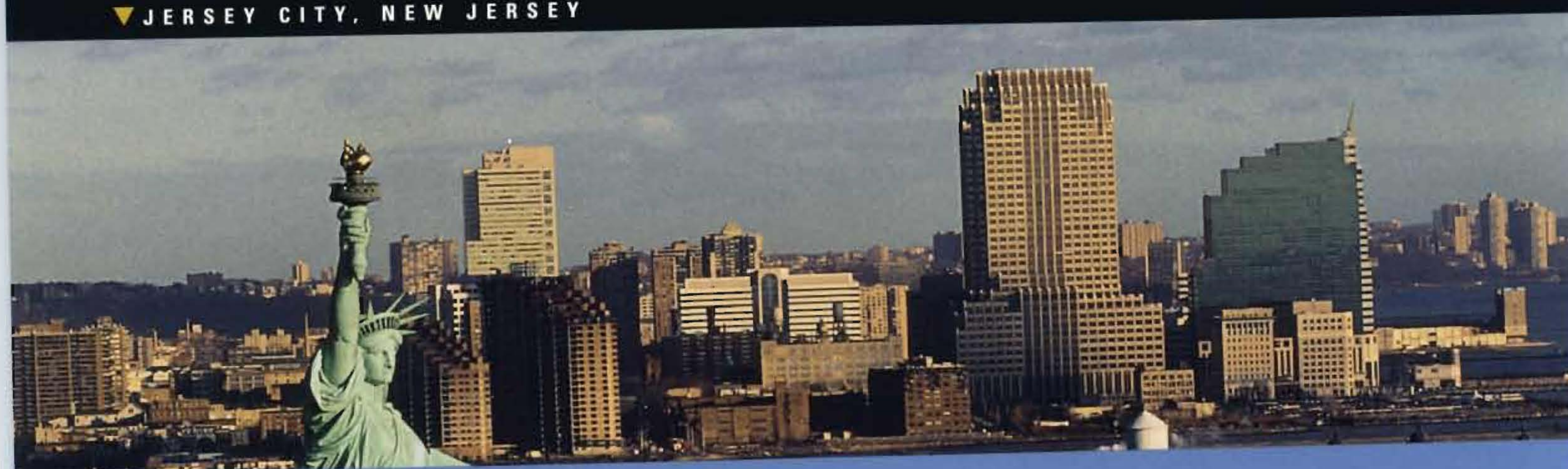
ATLANTA, GEORGIA

three of the nation's

HOUSTON, TEXAS

largest water systems

JERSEY CITY, NEW JERSEY



under private contract

Contract operations: strategy

In 1998 United Water through its affiliates won all four major contract operations awarded by the nation's cities: in Atlanta, Milwaukee, Gary, Indiana, and for the southern San Antonio area.

As a result, the company and its affiliates now operate three of the nation's largest municipal water operations under private contract—for Atlanta, Jersey City, New Jersey, southeastern Houston and outlying areas, and three of the country's largest municipal wastewater systems—in Milwaukee, Indianapolis and Gary.

United Water targets geographic regions where the company has a major presence and focuses on large-to-medium-size communities. The company also pursues contracts with smaller towns adjacent to or near areas served by its existing utilities or contract operations.

Largest Water Agreement

Under the Atlanta contract, the nation's largest water agreement, United Water's affiliate began supplying water to 1.5 million people in the city and 22 surrounding communities in January 1999. The company performs an array of services that include managing Atlanta's two water-treatment facilities and distribution system. It also handles billing, collections and customer service and is installing a premier computerized system to track and record all maintenance and repair bills.

Atlanta anticipates saving over $400 million, while United Water's affiliate and its 35.5 percent minority partner will receive nearly $430 million in revenues over the 20-year term of the contract.

United Water is achieving similar successes —and savings—in wastewater services.

EL SEGUNDO, CALIFORNIA

United Water's affiliate operates the world's largest water recycling program at a facility in El Segundo, California. The plant ultimately will recycle 100 million gallons of wastewater a day from a Los Angeles treatment plant and redistribute it for a wide range of irrigational and industrial uses.

Biggest Wastewater Contract

The Milwaukee contract is the biggest for a municipal wastewater system. Under the agreement, United Water's affiliate serves 1.2 million residents in two-dozen communities. The city expects to save over $140 million, while United Water's affiliate will receive approximately $300 million, over a 10-year period.

This is the most complex wastewater program under private contract. In addition to managing two large treatment facilities, the company operates major fertilizer and cogeneration plants, a sewer interceptor system and deep tunnel storage networks.

United Water extended its dominance in wastewater operations when Gary selected the company's affiliate to operate the city's wastewater facility and sewer system for 120,000 residents of Gary and its vicinity. The city will save an estimated $30 million, while United Water's affiliate and its equal partner will receive about $95 million, over the 10 years of the contract.

With these new contract operations, United Water is setting the pace in the fastest-growing segment of the water services industry, and in meeting the future water and wastewater needs of the nation's cities. This leadership is reinforced by the company's strengths in the contract operations business.

We also

▼MILWAUKEE, WISCONSIN

operate three of the

▼INDIANAPOLIS, INDIANA

country's largest

▼GARY, INDIANA

wastewater systems

United Water's strengths: leadership, track record,

HOBOKEN, NEW JERSEY, CONTRACT IS NATIONAL MODEL

size, expertise, management, labor relations,

ADVANCED SYSTEMS IMPROVE CUSTOMER SERVICE

EMPLOYEE TRAINING ENHANCES LABOR RELATIONS

customized programs, and customer service.

Contract operations: strengths

United Water's strengths help drive the company's success in gaining agreements for operating municipal water and wastewater systems. When seeking companies to manage their systems, cities are attracted by United Water's leadership in contract operations. Municipalities also value United Water's 129-year track record and national platform with operations throughout the country.

Global Corps of Experts

United Water augments these strengths with its strong management and a corps of experts from the company's utilities and contract operations, its United Water Services affiliate, and its strategic ally, Suez Lyonnaise des Eaux. In the United Kingdom, the company draws expertise from Northumbrian Water Group, in which United Water has had an investment since June 1996.

United Water has strong affiliates and allies. United Water Services is a leading contract operator of municipal water and wastewater systems in North America. Suez Lyonnaise des Eaux leads the world in water and wastewater services and research. Paris-based Suez Lyonnaise des Eaux has a market capitalization of over $31 billion, supplies drinking water to 77 million people and provides wastewater service to 52 million people around the world. And Northumbrian Water Group is a major investor-owned water services company that serves approximately four million people in the United Kingdom.

United Water benefited from this broad national and international expertise when it formed the team that prepared the winning proposal for the Atlanta contract.

Excellent Labor Relations

When mayors and city councils invite companies to submit plans for operating their systems, one of their most important concerns—labor relations—also is a United Water strength. United Water recognizes that developing strong, mutually beneficial relationships with labor is one of the most essential parts of a successful public-private partnership.

United Water through its affiliate has managed the Indianapolis wastewater system over the past four years and has built a positive relationship with the municipal union. Because of that excellent relationship, the local unit of the same union in Gary joined the company in its successful bid for the contract with the city.

And in 1996 United Water crafted an innovative agreement with Jersey City, New Jersey, which enabled the city's utility employees to remain employed by the city with full salaries, benefits and pensions.

United Water's unique labor agreements exemplify the company's history of innovation. Two years before the Jersey City contract, the company forged an agreement with Hoboken, New Jersey, that became a national model for water industry contracts.

These New Jersey agreements also reflect United Water's ability to customize programs throughout the country to meet the specific needs of cities and improve customer service. Looking ahead, United Water through its affiliate will meet these needs through the first contract ever awarded in the United States to design, build and operate an ultrafiltration plant. The facility, scheduled to be completed in December 1999, will treat water for 250,000 people in the southern San Antonio area. The project is part of a 10-year, $30 million agreement.

This spirit of innovation also is a hallmark of the company's regulated utilities.

(Above) United Water invests in water-related business such as Northumbrian Water Group (NWG), a major investor-owned water services company in the United Kingdom. NWG owns and operates these water-clarifying tanks.

(Below) The strategic alliance with Suez Lyonnaise des Eaux augments United Water's expertise and resources. The Paris-based company is the world leader in water and wastewater services and research.

Utilities:

innovation, strength, stability

United Water's utilities have established a long history of innovation. Water treatment initiatives range from the use of rapid-sand filtration in 1904 to the large-scale use of ozone technology in 1989. The company was among the first to build dams and reservoirs that serve northern New Jersey and southern New York State and to have the foresight to protect the watershed.

Technological innovations are among the strengths that contribute to United Water's leading position in the water services business. The company also continuously implements operational and managerial efficiencies that help reduce operating costs among its regulated utilities.

Geographic Diversity

The geographic diversity of United Water's utilities enables the company to offset earnings impacted by adverse weather in one area of the country with earnings in regions with favorable conditions.

These strengths contribute to United Water's stability and its ability to advance the company's utility growth strategy. This strategy calls for sustaining customer growth, pursuing water-related acquisitions, and filing for rate increases when needed.

Cost Controls

United Water's utility strategy also aims to improve earnings by reducing the cost of providing service through efficiency and productivity gains. In 1998 the company launched a new phase of its computerized, integrated financial management system. This new technology allows the company to perform more functions on a centralized basis and to focus on achieving efficiencies and cost savings.

Located near Wilmington, Delaware, this inflatable rubber dam exemplifies United Water's historic role as a technological innovator. The dam, which can be inflated to capture fresh water and deflated to return the stream to its normal flow, is the first to be used in North America to ensure a drinking water supply.

United Water has the unique capability to check the accuracy and performance of large, commercial meters, such as these being tested at the company's facility in Hackensack, New Jersey.

utilities: innovation, strength, stability continued

Together with the new financial management system, United Water implemented the next step of its activity-based costing system, which enhances the ability to analyze and control the costs of performing core utility activities. The company also instituted a new customer information system. United Water expects to achieve long-term improvements in productivity from these systems.

In addition, the company seeks other ways to achieve savings, such as reducing financing costs. In 1998 United Water refinanced a substantial portion of utility debt.

United Water continually pursues acquisitions as part of its utility strategy. In early 1999 the company acquired a water system that increased its customer base in Boise, Idaho, and accelerated United Water's expansion in the fast-growing Boise area. So far this decade, United Water has acquired over 20 water and wastewater operations throughout the country.

Strengthening the company's utilities and acquiring new water-related operations, along with expanding through contract operations and with strategic allies, form the basis for United Water's growth strategy. That strategy led to the company's 1998 successes, and will generate new successes well into the next century.

Financial Contents

Significant Items

The following items had a significant impact on the financial results of United Water Resources (United Water, or the Company):

Investment in United Water Services: On July 28, 1997, United Water Services, a 50/50 joint venture between United Water and Suez Lyonnaise des Eaux acquired the remaining 50% stake in JMM Operational Services.

United Water Services provides contract operations and maintenance services for water and wastewater facilities and is pursuing additional contract operations. As a result, United Water Services was awarded several contracts. The largest awards include a ten-year contract to operate the wastewater systems in Milwaukee, Wisconsin, and a 20-year contract to operate the water system in Atlanta, Georgia, with a minority partner. United Water Services also operates a meter installation subsidiary, United Metering, which it purchased from United Water in December 1997 for book value of $6.2 million.

In July 1997, the Company also acquired a 30% and a 20% interest in United Water Services Canada (UWS Canada) and United Water Services Mexico (UWS Mexico), respectively. In December 1998, United Water purchased additional interests and now has a 33.3% and a 20.5% interest in UWS Canada and UWS Mexico, respectively.

At December 31, 1998 and 1997, United Water had equity investments, relating to contract services, of approximately $19.8 million and $20.2 million, respectively, including investments in Canada and Mexico. This amount is included in equity investments in the accompanying consolidated balance sheet. United Water's share of earnings in these investments is included in equity earnings of affiliates in the accompanying statement of consolidated income.

Investment in Northumbrian Partnership: On June 28, 1996, United Water and Lyonnaise Europe (a wholly-owned subsidiary of Suez Lyonnaise des Eaux) formed the Northumbrian Partnership (the Partnership), an equal partnership which has acquired a 20% interest in Northumbrian Water Group plc (NWG), a major investor-owned water and wastewater company in the United Kingdom. United Water's initial $62 million investment in the Partnership was made through its wholly-owned subsidiary in the United Kingdom, United Water UK Limited. Investment in the Partnership was $96.3 million and $78.7 million at December 31, 1998 and 1997, respectively, and is included in equity investments in the consolidated balance sheet. United Water's share of the Partnership's earnings, which totaled $17.1 million and $13.6 million in 1998 and 1997, respectively, is included in equity earnings of affiliates in the accompanying statement of consolidated income.

During 1997, the United Kingdom's new Labor Government imposed a one-time "windfall profits" tax on privatized utilities. The levying of this one-time tax negatively impacted the Company's earnings from its investment in NWG by $13.1 million, which was partially offset by the effect of a change in the tax rate on deferred taxes of $2.8 million. The result was a net impact of $10.3 million. The imposition of this tax had been factored into the Company's financial analysis at the time of its investment in NWG and was considered in determining the purchase price. The tax did not have an effect on United Water's cash flow or ability to pay dividends, nor did it affect the long-term benefit the Company expected to derive from its investment in NWG.

Discontinued Operations: In December 1996, the Company announced its intention to dispose of its environmental testing business, Laboratory Resources, a wholly-owned subsidiary of the Company, closing its operations in Teterboro, New Jersey. Subsequently, in January 1997, it sold its laboratory facility in Brooklyn, Connecticut. The Company accounted for this disposal in accordance with the provisions of Accounting Principles Board Opinion No. 30, "Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual, and Infrequently Occurring Events and Transactions". The subsidiary had been operating in a very competitive environment over a prolonged period of time and had not contributed to the Company's earnings, with a net loss of $1.5 million in 1996. The operating results of Laboratory Resources prior to the date of discontinuance are shown separately in the accompanying statement of consolidated income and all of the financial statements of prior periods have been restated to reflect the discontinuance of Laboratory Resources' operations. See Note 14 to the consolidated financial statements for further details.

Transfer of New Mexico Operations: United Waterworks owned a utility subsidiary which provided water and wastewater services to customers in Rio Rancho, New Mexico. In April 1995, the city of Rio Rancho (the City) and the Company's utility subsidiary entered into an original stipulation in settlement of a condemnation action and on June 30, 1995, the City assumed possession of the operations of the utility subsidiary. The original stipulation was contested by various parties, but the City retained possession of the utility's operations.

On March 29, 1996, the Company fully settled the condemnation proceeding with the City. Under the terms of the agreement, the Company accepted $67 million for the water and wastewater systems of its New Mexico operations. This transaction resulted in an after-tax gain of $4.3 million which is included in the Company's 1996 earnings.

Liquidity and Capital Resources

As shown in the consolidated statement of cash flows, the Company's major uses of cash in 1998 included: $106 million of capital expenditures and $38.5 million of common, preferred and preference dividends paid to shareholders. The major sources of funds to meet these cash needs included: $85.2 million of additional long-term debt; $80.2 million of cash provided by operations; $23.1 million of proceeds from the issuance of additional shares of common stock; and an $18.5 million increase in short-term notes payable.

Capital expenditures are generally incurred by United Water's utility subsidiaries in connection with the normal upgrading and expansion of existing water and wastewater facilities and to comply with existing environmental regulations. United Water considers its utility plant to be adequate and in good condition. These capital expenditures are necessary to meet growth requirements and to comply with environmental laws and regulations. Excluding the effects of inflation, the capital expenditures of United Water's utility subsidiaries are projected to aggregate $262 million over the next five years, including $57 million and $58 million in 1999 and 2000, respectively. This total includes $165 million for United Waterworks and $92 million for United Water New Jersey and United Water New York. The expenditures related to compliance with environmental laws and regulations are estimated to be approximately 25% of the projected capital expenditures over the 1999-2003 period. To the best of management's knowledge, the Company is in compliance with all major environmental laws and regulations.

United Water anticipates that its future capital expenditures will be funded by internally generated funds, external debt financings and the issuance of additional common and preferred stock, including shares issued to existing shareholders, bondholders, customers, and employees under the Company's dividend reinvestment and stock purchase plans. In addition, United Water's regulated utilities participate in a number of tax-exempt financings to fund capital expenditures. The companies draw down funds on these financings as qualified capital expenditures are made. As of December 31, 1998, $48.5 million of proceeds from these financings had not yet been disbursed to the Company and are included in the consolidated balance sheet as restricted cash. The amount and timing of the use of these proceeds and of future financings will depend on actual capital expenditures, the timeliness and adequacy of rate relief, the availability and cost of capital, and the ability to meet interest and fixed charge coverage requirements.

In June 1997, United Water issued $40 million of 7.45%-7.9% Senior Notes ($15 million due 2007 and $25 million due 2022). Proceeds from the notes were used to refinance existing short-term debt of the Company.

In August 1997, United Waterworks issued $20 million of 5.3% tax-exempt Water Resource Development Revenue Bonds, due 2027, through the Idaho Water Resource Board. The proceeds are being used to finance a portion of the costs of certain facilities to be owned by United Water Idaho (a subsidiary of United Waterworks).

In December 1994, United Waterworks entered into a medium-term note program that enabled United Waterworks to issue up to $75 million of debt with terms ranging from 9 months to 30 years. The interest rates are set as notes are issued under the program. The first $10 million of notes under this program were issued in 1995. In October 1997, United Waterworks issued $15 million of notes under this program, at a rate of 6.8%, with the full amount maturing in 2007. In February 1998, United Waterworks issued an additional $40 million of notes ($20 million at 6.97% due 2023, $15 million at 7.1% due 2028 and $5 million at 6.9% due 2017). In November 1998, United Waterworks issued the final $10 million of notes under this program ($5 million at 6.44% due 2008 and $5 million at 6.97% due 2023). The proceeds were used to redeem outstanding notes payable.

In June 1996, United Water entered into a $30 million long-term note agreement with Credit Lyonnais to partially fund its investment in the Northumbrian Partnership. The loan bears interest at a London Interbank Offered Rate (LIBOR)-based floating rate and is payable in annual installments through June 2006. In December 1998, the Company entered into an interest rate swap agreement which fixed the interest rate at 5.24% for 1999 and 5.34% for the years 2000 through 2003.

In December 1998, United Water New Jersey issued $35 million of 5% Water Facilities Revenue Bonds through the New Jersey Economic Development Authority due 2028. The proceeds are being used to finance the cost of acquiring, constructing and reconstructing certain water transmission, transportation, storage, treatment, and distribution facilities located in Passaic, Bergen, Sussex, and Hudson counties in New Jersey.

In January 1999, United Water issued $30 million of Senior Notes ($5 million at 6.07% due 2005, $10 million at 6.43% due 2009, $10 million at 6.7% due 2019, and $5 million at 7.04% due 2019). The proceeds were used to redeem all remaining shares of 7⅝% Series B cumulative preferred stock. See Note 7 to the consolidated financial statements for further details.

At December 31, 1998, United Water had cash and cash equivalents of $8 million (excluding restricted cash) and unused short-term bank lines of credit of $186.4 million. Management expects that cash flows provided by operations, unused credit lines currently available and cash generated from the dividend reinvestment and stock purchase plans will be sufficient to meet anticipated future operational needs.

Year 2000 Compliance

Overview: United Water is implementing a Year 2000 (Y2K) program designed to mitigate, to the fullest extent possible, the impact of the century date change on the Company's computer systems and automated processes, including those that affect the delivery of water and wastewater services. The Company initiated this program in 1994 with the Information Technology Strategic Plan (the ITSP), which addressed all areas of technology and automation within United Water. A key component of that plan was the identification of the Y2K problem and the need to address Y2K issues affecting all aspects of the Company's operations. With respect to each project or initiative undertaken at United Water since 1994 that has Y2K ramifications, the Company has addressed "Y2K readiness" as a critical component of that project.

United Water defines Y2K readiness as the ability of the Company to advance into the next century with minimal effect on the Company's critical computer systems and automated processes that control the delivery of water and wastewater services, and affect the Company's operations, liquidity or financial condition.

The Y2K program addresses internal systems and processes consisting of application software, hardware, databases, networks, personal computers, data processing equipment and operating systems (collectively, information technology or IT systems) and embedded technology or microprocessors in non-computer equipment (collectively, non-IT systems). The Y2K program also addresses the assessment and monitoring of the Y2K compliance status of third parties upon which the Company relies. This program encompasses the following five phases: 1) survey and inventory, 2) assessment of risk, including the identification and survey of critical vendors and service providers, 3) remediation of non-compliant systems, including the replacement of aging legacy applications, 4) testing and validation of the remediation efforts, and 5) contingency planning and related testing.

In addition, management believes that United Water has complied with the various Y2K requirements of the regulatory agencies that supervise its activities. Such compliance includes responding to surveys and questionnaires, filing status reports, participating in task forces and subcommittees for the purpose of meeting Y2K readiness targets, and contingency planning efforts.

The Company's State of Readiness: Consistent with the five phases of the Y2K program, the primary element in United Water's Y2K readiness strategy has been to replace aging IT and non-IT systems, where necessary. This strategy evolved from ITSP which, independent of the Y2K program, identified the need to replace technical infrastructure, including IT and non-IT systems, in order to position United Water and its operating affiliates for a smooth transition into the 21st century. In addition to replacement activities, the Company has also undertaken remediation efforts to upgrade, repair and improve existing IT and non-IT systems where appropriate. These efforts are intended to result in the replacement and upgrading of IT and non-IT systems critical to the operation of the Company, including the provision of water and wastewater services, financial applications, customer information systems and operational systems, such as the Supervisory Control and Data Acquisition System (SCADA), which monitors and controls industrial processes.

In addition, United Water is currently refining contingency plans and related tests to further mitigate the risk of service interruptions at each of its locations. These contingency plans have been developed, and the testing of each plan is anticipated to be completed by the end of the first quarter of 1999. The major focus of the contingency plans is to address the possibility of automation failure of critical vendors and service providers so that the Company can sustain its operational systems in the event of any such failure.

As of December 31, 1998, the status of the Company's progress toward completion of the five phases of the Y2K program was as follows: 1) survey and inventory: IT 100%, non-IT 100%; 2) assessment of risk: IT 99%, non-IT 99%; 3) remediation: IT 93%, non-IT 93%; 4) testing: IT 50%, non-IT 50%; and 5) contingency planning: IT 60%, non-IT 60%. All replacements and upgrades are scheduled to be completed by the end of the second quarter of 1999.

In addition to its own Y2K program, the Company has been involved with Y2K compliance efforts undertaken by one of its equity investments, United Water Services (UWS).

UWS, which is engaged in providing contract operations to U.S. cities, is implementing a Y2K program following the guidelines established by the Company. This program has been applied to all UWS's project sites and has resulted in the production of inventories, risk assessments, testing methodologies and contingency plans for Y2K compliance. All systems are expected to be finalized and tested by the end of the second quarter of 1999.

Where UWS has assumed responsibility for part or all of the Y2K compliance efforts of its operating affiliates in the various cities, it is actively coordinating Y2K corrective measures with the cities and their Y2K consultants or representatives, where applicable, to mitigate business interruption exposures associated with the Y2K problem.

United Water is maintaining close contact with UWS and other entities in which it has equity interests to ascertain that appropriate and prudent action is being taken in order to achieve Y2K compliance.

Relationships with Third Parties: United Water has identified the following third party relationships to be addressed as part of the Y2K program: regulatory agencies, critical vendors and service providers.

United Water is in continuous communication with appropriate regulatory agencies regarding the Y2K issue. All requests for information and status reports, as well as other specific regulatory requirements are handled on a priority basis. Management believes that the Company is in compliance with all regulatory matters relating to Y2K.

The Company has contacted its critical vendors and service providers to determine the degree of their Y2K readiness. The responses received to date indicate that those vendors and service providers either are or will be Y2K compliant. The status of those vendors and service providers who have either not responded or are not yet compliant is being tracked closely. The electric power and telecommunications industries have been identified as the most critical service providers for the water industry. In the localities in which United Water operates, it is closely monitoring the progress of the local electric power and telecommunications companies and will continue to scrutinize the progress of these providers. The Company is actively monitoring the Y2K compliance status of its critical vendors and service providers and has received approximately 75% of responses. The Company intends to continue monitoring these critical vendors and service providers through its transition into the 21st century.

Costs: United Water's Y2K readiness evolved from the strategic initiatives of the ITSP which was budgeted as part of the Company's ongoing capital expenditures since 1994. As a result, United Water has been able to keep to a minimum expenses related to Y2K compliance outside of the ITSP budget. The Company's principal technology costs to date have been associated with the planned replacement of IT and non-IT systems, which has not been accelerated due to the Y2K issue.

United Water estimates its costs to date related to Y2K compliance efforts that fall outside the ITSP budget are approximately $.2 million. Additional non-ITSP budgeted costs expected to be incurred over the remainder of the program are estimated to be $.7 million. These costs include SCADA upgrade as required, internal employee time, as well as other miscellaneous costs.

Risks: The most reasonably likely worst case scenarios due to Y2K noncompliance issues would be fluctuations in water pressure, aesthetic water quality and other temporary service interruptions. This would be attributable to third party failures including electric power and telecommunications outages.

In addition, a Y2K failure from any of the Company's large equity investments including its investment in the Northumbrian Partnership, could have a detrimental effect on the Company's results of operations.

The estimates and conclusions included in the Y2K update are based on management's best estimates of future events. The risks involved in completing Y2K compliance include the availability of resources, unanticipated problems identified in the ongoing compliance review and the ability of outside vendors and service providers to be Y2K compliant.

Contingency Plans: The primary elements of contingency planning include procurement of back-up energy sources, typically adding portable power generators where appropriate, deployment of key personnel on critical dates relating to the century date change and providing for the efficient flow of communication both internally and externally in the event of interruption of service during critical dates relating to the century date change.

Rate Matters

The profitability of United Water's regulated utilities is, to a large extent, dependent upon adequate and timely rate relief. The Company anticipates that the regulatory authorities that have jurisdiction over its utility operations will allow the Company's regulated utilities to earn a reasonable return on their utility investments.

The Company continues to follow Statement of Financial Accounting Standards (SFAS) No. 71, "Accounting for the Effects of Certain Types of Regulation," for its regulated utilities. SFAS No. 71 provides for the recognition of regulatory assets and liabilities as allowed by state regulators that are considered probable of recovery. See Note 1 to the consolidated financial statements.

During 1998, the Company's regulated utilities received fourteen rate decisions with an aggregate annual revenue increase of $8.7 million, which includes $2.4 million in increased revenues effective on an interim basis for United Water Delaware. An estimated $4.7 million of this amount was reflected in 1998's revenues while the remaining $4 million is expected to increase revenues in 1999. Current year revenues also reflect the carryover impact of the rate awards granted in 1997 in the amount of $5.1 million. See Note 11 to the consolidated financial statements for further details.

At the end of January 1999, the Company had five rate cases pending requesting an aggregate annual rate increase of $10.9 million. The most significant rate cases pending were filed by United Water Florida and United Water Delaware. These filings were made to meet increased investment in utility plant and higher operation and maintenance costs. In May 1998, United Water Florida applied to the Florida Public Service Commission for rate relief in the amount of $2.2 million, or 24.3%, in water revenues and $3.1 million, or 18.7%, in wastewater revenues. A decision on the United Water Florida application is expected before the end of the first quarter of 1999.

On March 11, 1998, United Water Delaware applied to the Delaware Public Service Commission for rate relief in the amount of $4.1 million, or 24.8%, in water revenues. On May 11, 1998, interim rates of $2.4 million were placed in effect, subject to refund. A decision on this application is expected before the end of the second quarter of 1999. The Company believes the outcome of this application will not have a material effect on earnings.

On October 26, 1996, United Water Delaware placed $2.3 million in increased revenues in effect, subject to refund. On July 15, 1997, the Delaware Public Utility Commission granted the Company a permanent rate increase of $1.6 million. On July 16, 1997, the Company filed an appeal and application for a stay of the Commission's Order. On July 29, 1997, the Delaware Superior Court granted a stay of the Commission decision pending the appeal. On March 31, 1998, the Superior Court decided in favor of the Commission. The Company appealed this decision to the Supreme Court of Delaware and on February 11, 1999, the Supreme Court reversed the Commission's decision which denied the $.7 million annual revenue increase, subject to refund and remanded the matter to the Commission. The Company expects that the Commission will enter an Order on remand which will eliminate the prospect of refunding any part of the $2.3 million.

The Company has requested and received recovery of its regulatory assets for postretirement benefits other than pension as well as the recognition of the current expense for these benefits for the majority of its regulated subsidiaries. The regulatory assets are expected to be recovered over an average period of 15 years. At December 31, 1998, three regulated subsidiaries were awaiting decisions from the applicable commissions. Management believes it will receive favorable decisions on the pending cases prior to the end of 1999.

Generally, the rate awards actually received by the Company's operating utilities are less than the amounts requested, primarily due to differing positions of the parties involved and/or updated information provided during the proceedings.

Real Estate Activities

United Properties Group (United Properties) owns and manages a portfolio of real estate located in New Jersey, New York, Delaware, Idaho, and Florida, consisting of commercial properties, golf courses and land under development.

United Properties expects to spend $25.9 million over the next five years for capital expenditures on its existing real estate portfolio, including $8.3 million and $6.9 million in 1999 and 2000, respectively. Funding for United Properties' activities is anticipated to come from sales of properties, operations of existing commercial properties and golf courses, and proceeds from new financings. The timing of these expenditures will depend upon market conditions and the attainment of necessary approvals.

Results of Operations

Overview: United Water's net income applicable to common stock for 1998 was $43.9 million, or $1.19 per common share, as compared to $29.3 million, or $.83 per common share, earned in 1997. Earnings for 1997 included a net $10.3 million charge resulting from the "windfall profits" tax in the United Kingdom. Income before non-recurring items was $43.9 million, or $1.19 per common share for 1998 compared with $39.7 million, or $1.12 per common share for 1997. This increase was attributable to improved domestic utility performance as a result of rate awards, higher water consumption and a property tax settlement relating to a prior year. In addition, the Company experienced higher earnings from the Northumbrian Partnership primarily due to the effect on deferred taxes of a decrease in the UK corporate tax rate.

United Water's net income applicable to common stock for 1997 was $29.3 million, or $.83 per common share, as compared to $34 million, or $1.01 per common share, earned in 1996. Earnings for 1997 included a net $10.3 million charge resulting from the "windfall profits" tax in the United Kingdom. Income from continuing operations and before non-recurring items was $39.7 million, or $1.12 per common share for 1997 compared with $34.1 million, or $1.01 per common share for 1996. This increase was attributable to a $6 million increase in equity earnings of affiliates during 1997, which resulted from a full year of operations in the United Kingdom. Earnings for 1996 included a one-time, after-tax gain of $4.3 million, or $.13 per common share, resulting from a condemnation settlement in New Mexico which was offset by a charge relating to the discontinuance of the Company's environmental testing business.

Operating Revenues: Operating revenues increased $4.8 million, or 1.4%, in 1998 and $19.4 million, or 5.8%, in 1997 from the prior years, as follows:

(THOUSANDS OF DOLLARS)	1998 VS. 1997 INCREASE (DECREASE)		1997 VS. 1996 INCREASE (DECREASE)	
Utilities:				
Rate awards	$ 9,790	2.8%	$10,650	3.2%
Consumption	1,346	0.4%	137	0.0%
Growth	993	0.3%	3,276	1.0%
Real estate	(3,879)	(1.1%)	6,306	1.9%
Other operations	(3,449)	(1.0%)	(1,005)	(0.3%)
	$ 4,801	1.4%	$19,364	5.8%

1998 versus 1997: The 2.8% increase in revenues from rate awards in 1998 includes the impact of fifteen 1997 and fourteen current year increases for the Company's operating utilities. Higher consumption due to favorable weather conditions in northeast service areas resulted in an increase in revenues of $1.3 million in 1998. The increase in revenues due to growth is partially attributable to increased customers at several operating utilities. Real estate revenues decreased $3.9 million primarily due to lower land sale revenues as a result of a significant land sale in the first quarter of 1997, partially offset by higher golf course revenues. The $3.4 million decrease in operating revenues from other operations was primarily attributable to the absence of revenues from the Company's meter installation subsidiary, which was sold in the fourth quarter of 1997, partially offset by an increase in revenues from the public-private partnership with Jersey City, New Jersey.

1997 versus 1996: The 3.2% increase in revenues from rate awards in 1997 includes the impact of ten 1996 and fifteen 1997 increases for the Company's operating utilities. The increase in revenues due to growth is partially attributable to the acquisitions of two utilities in New Jersey in the second quarter of 1996 as well as increased customers at several operating utilities. Real estate revenues were higher as compared to 1996, primarily due to a $5.8 million increase in property sales, which included a significant land sale, in addition to higher golf course revenues. The $1 million decrease in operating revenues from other operations was primarily attributable to lower revenues from meter installation contracts, partially offset by the benefit of a full year of operations from the public-private partnership with Jersey City, which commenced in May 1996. In December 1997, United Water sold United Metering, its meter installation subsidiary, to United Water Services. As a result, United Water retains 50% ownership in United Metering.

Operating Expenses: Operating expenses increased $2.8 million in 1998 and $19.4 million in 1997 from the prior years, as follows:

(THOUSANDS OF DOLLARS)	1998 VS. 1997 (DECREASE) INCREASE		1997 VS. 1996 INCREASE	
Operation and maintenance	$ (560)	(0.3%)	$13,069	8.4%
Depreciation and amortization	5,256	15.1%	3,842	12.5%
General taxes	(1,851)	(3.6%)	2,508	5.1%

1998 versus 1997: The decrease in operation and maintenance expenses was due primarily to the absence of costs from the Company's meter installation subsidiary, which was sold in the fourth quarter of 1997 as well as a $3.9 million decrease in the cost of real estate properties sold, primarily due to a significant land sale in the first quarter of 1997. This was partially offset by the write-off of deferred start-up charges under Statement of Position 98-5, "Reporting on the Costs of Start-Up Activities" as well as higher outside services and employee benefits costs at several of the Company's subsidiaries.

The $5.3 million increase in depreciation and amortization was primarily attributable to utility plant additions by the Company's utility subsidiaries, as well as accelerated amortization associated with the service contract in Jersey City.

General taxes decreased $1.9 million, or 3.6%, in 1998 primarily due to a property tax settlement received in the fourth quarter of 1998. This was partially offset by higher real estate, franchise and gross receipts taxes in utility operations.

1997 versus 1996: The increase in operation and maintenance expenses was due primarily to a $2.6 million increase in the cost of real estate properties sold, $2.4 million in additional operating expenses as a result of a full year of operations of the public-private partnership with Jersey City, higher outside services and employee benefits costs at several of the Company's subsidiaries, and additional operating expenses incurred relating to the acquisitions of two utilities in New Jersey in May 1996. These increases were partially offset by lower costs from meter installation contracts.

The $3.8 million increase in depreciation and amortization was primarily attributable to utility plant additions by United Waterworks' utility subsidiaries, as well as amortization associated with the service contract in Jersey City.

General taxes increased $2.5 million, or 5.1%, in 1997 primarily due to higher real estate, franchise and gross receipts taxes in utility operations.

Interest Expense: Interest expense increased $.5 million in 1998 and $.4 million in 1997 compared to prior years. See the statement of consolidated capitalization and Note 4 to the consolidated financial statements for further details on long-term debt and notes payable.

Equity Earnings of Affiliates: The $.8 million increase in equity earnings of affiliates in 1998 was due mainly to a $3.5 million increase in earnings from the Northumbrian Partnership which resulted primarily from the effect on deferred taxes of a decrease in the UK corporate tax rate.

This was partially offset by a $2.2 million decrease in combined earnings from United Water Services, UWS Canada and UWS Mexico. This decrease was primarily attributable to business development costs associated with ongoing efforts to expand contract operations. One of the successes resulting from these efforts came in November 1998, when United Water Services was awarded a 20-year contract, with annual revenues of $21.4 million, to operate the water system in Atlanta, Georgia, with a minority partner. The Company also experienced lower equity earnings as a result of a one-time condemnation settlement by its other equity investment, Dundee Water Power and Land.

Income Taxes: The effective income tax rates on income before preferred and preference stock dividends were 27.9% in 1998, 36.4% in 1997 and 36.5% in 1996. An analysis of income taxes is included in Note 12 to the consolidated financial statements.

New Accounting Standards: In June 1998, the Financial Accounting Standards Board issued SFAS No. 133, "Accounting for Derivatives and Hedging Activities" effective for all fiscal years beginning after June 15, 1999. SFAS No. 133 requires that all derivative instruments be recorded on the balance sheet at their fair value. Changes in the fair value of derivatives are recorded each period in current earnings or other comprehensive income. Due to its limited use of derivative instruments, management believes the adoption of SFAS No. 133 will not have a significant effect on the Company's financial position or results of operations.

Effects of Inflation: Operating income from utility operations is normally not materially affected by inflation because cost increases generally lead to proportionate increases in revenues allowed through the regulatory process. However, there is a lag in the recovery of higher expenses through the regulatory process, and therefore, high inflation could have a detrimental effect on the Company until rate increases are received. Conversely, lower inflation and lower interest rates tend to result in reductions in the rates of return allowed by the utility commissions, as has occurred over the last several years.

Prospective Information: In addition to the historical information contained herein, this report contains a number of "forward-looking statements," within the meaning of the Securities Exchange Act of 1934. Such statements address future events and conditions concerning the adequacy of water supply and utility plant, capital expenditures, earnings on assets, resolution and impact of litigation, liquidity and capital resources and accounting matters. Actual results in each case could differ materially from those projected in such statements, by reason of factors including, without limitation, general economic conditions, competition, actions by regulators and other governmental authorities, and technological developments affecting the Company's operations, markets, services and prices, and other factors discussed in the Company's filings with the Securities and Exchange Commission, including this report.

Consolidated Balance Sheet

DECEMBER 31, (THOUSANDS OF DOLLARS)	1998	1997
Assets		
Utility plant, including $47,348 and $49,301 under construction	$1,540,564	$1,439,854
Less accumulated depreciation	328,224	296,820
	1,212,340	1,143,034
Utility plant acquisition adjustments,		
Less accumulated amortization of $11,411 and $9,527	61,320	63,026
Real estate and other investments,		
Less accumulated depreciation of $13,628 and $11,497	81,630	79,487
Equity investments	116,598	99,197
	198,228	178,684
Current assets:		
Cash and cash equivalents	8,011	8,546
Restricted cash	48,495	34,581
Accounts receivable and unbilled revenues, less allowance of $1,204 and $2,528	59,693	57,723
Prepaid and other current assets	12,235	11,705
	128,434	112,555
Deferred charges and other assets:		
Regulatory assets	76,548	79,748
Prepaid employee benefits	29,237	21,426
Unamortized debt expense	34,745	31,019
Other deferred charges and assets	28,270	28,850
	168,800	161,043
	$1,769,122	$1,658,342
Capitalization and Liabilities		
Capitalization:		
Common stock and retained earnings	$ 456,029	$ 418,601
Preferred stock without mandatory redemption	9,000	9,000
Preferred stock with mandatory redemption	49,748	51,838
Preference stock, convertible, with mandatory redemption	30,534	34,741
Long-term debt	652,969	622,737
	1,198,280	1,136,917
Current liabilities:		
Notes payable	93,400	74,925
Preferred stock and long-term debt due within one year	5,795	8,022
Accounts payable and other current liabilities	36,525	32,833
Accrued taxes	24,257	26,878
Accrued interest and dividends	8,023	8,117
	168,000	150,775
Deferred credits and other liabilities:		
Deferred income taxes and investment tax credits	195,368	183,490
Customer advances for construction	30,648	27,356
Contributions in aid of construction	143,327	133,684
Other deferred credits and liabilities	33,499	26,120
	402,842	370,650
Commitments and contingencies (Notes 6 and 11)		
	$1,769,122	$1,658,342

The accompanying notes are an integral part of these consolidated financial statements.

Statement of Consolidated Income

YEARS ENDED DECEMBER 31, (THOUSANDS EXCEPT PER SHARE DATA)	1998	1997	1996
Operating revenues	$356,210	$351,409	$332,045
Operating expenses:			
Operation and maintenance	168,387	168,947	155,878
Depreciation and amortization	39,950	34,694	30,852
General taxes	50,273	52,124	49,616
Total operating expenses	258,610	255,765	236,346
Operating income	97,600	95,644	95,699
Interest and other expenses:			
Interest expense, net of amount capitalized	45,917	45,372	44,951
Allowance for funds used during construction	(4,567)	(3,397)	(3,355)
Preferred stock dividends of subsidiaries	2,223	2,256	2,277
Gain on New Mexico settlement	—	—	(10,372)
Windfall profits tax of affiliate	—	10,334	—
Equity earnings of affiliates	(11,451)	(10,647)	(4,617)
Other income, net	(1,959)	(2,529)	(2,083)
Total interest and other expenses	30,163	41,389	26,801
Income from continuing operations before income taxes	67,437	54,255	68,898
Provision for income taxes	19,450	20,579	25,878
Income from continuing operations	47,987	33,676	43,020
Preferred and preference stock dividends	4,058	4,345	4,613
Net income applicable to common stock from continuing operations	$ 43,929	$ 29,331	$ 38,407
Discontinued operations:			
Loss from discontinued operations, net of income tax benefit of $824	—	—	(1,532)
Loss on disposal of discontinued business, net of income tax benefit of $1,543	—	—	(2,865)
Loss from discontinued operations	—	—	(4,397)
Net income applicable to common stock	$ 43,929	$ 29,331	$ 34,010
Average common shares outstanding	37,028	35,492	33,707
Net income (loss) per common share			
Continuing operations	$ 1.19	$ .83	$ 1.14
Discontinued operations	—	—	(.13)
Total	$ 1.19	$ .83	$ 1.01
Average common shares outstanding—assuming dilution	39,192	37,838	36,218
Net income (loss) per common share			
Continuing operations	$ 1.17	$ .83	$ 1.12
Discontinued operations	—	—	(.12)
Total	$ 1.17	$ .83	$ 1.00

The accompanying notes are an integral part of these consolidated financial statements.

Statement of Consolidated Common Equity

(THOUSANDS)	COMMON STOCK NUMBER OF SHARES	COMMON STOCK AMOUNT	CUMULATIVE TRANSLATION ADJUSTMENT	RETAINED EARNINGS
Balance at December 31, 1995	32,880	$304,663	—	$ 53,639
Dividend reinvestment and stock purchase plans	1,375	18,845	—	—
Cumulative translation adjustment	—	—	$6,703	—
Conversion of 5% preference stock	294	4,624	—	—
Net income applicable to common stock	—	—	—	34,010
Cash dividends paid on common stock, $.92 per share	—	—	—	(30,994)
Balance at December 31, 1996	34,549	328,132	6,703	56,655
Dividend reinvestment and stock purchase plans	1,446	25,083	—	—
Cumulative translation adjustment	—	—	591	—
Conversion of 5% preference stock	300	4,742	—	—
Net income applicable to common stock	—	—	—	29,331
Cash dividends paid on common stock, $.92 per share	—	—	—	(32,636)
Balance at December 31, 1997	36,295	357,957	7,294	53,350
Dividend reinvestment and stock purchase plans	1,264	23,068	—	—
Cumulative translation adjustment	—	—	464	—
Conversion of 5% preference stock	277	4,394	—	—
Net income applicable to common stock	—	—	—	43,929
Cash dividends paid on common stock, $.93 per share	—	—	—	(34,427)
Balance at December 31, 1998	37,836	$385,419	$7,758	$ 62,852

The accompanying notes are an integral part of these consolidated financial statements.

Statement of Consolidated Cash Flows

YEARS ENDED DECEMBER 31, (THOUSANDS OF DOLLARS)	1998	1997	1996
Operating activities:			
Net income	$ 47,987	$ 33,676	$ 38,623
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	41,300	35,959	32,068
Deferred income taxes and investment tax credits, net	11,878	8,934	18,399
Gain on New Mexico settlement	—	—	(10,372)
Equity earnings of affiliates	(11,451)	(313)	(4,617)
Proceeds from sale of United Metering	—	6,223	—
Proceeds from sales of properties	3,761	11,068	4,385
Gain on sales of properties	(2,605)	(5,220)	(935)
Improvements to property under development	(2,125)	(1,376)	(1,333)
Loss on disposal of discontinued operations	—	—	4,408
Allowance for funds used during construction	(4,567)	(3,397)	(3,355)
Changes in assets and liabilities, net of effect of New Mexico settlement and acquisitions:			
Accounts receivable and unbilled revenues	(1,970)	2,551	(3,729)
Prepayments	(530)	(311)	3,397
Prepaid employee benefits	(7,811)	(5,287)	(3,757)
Regulatory assets	3,200	(4,569)	(8,821)
Accounts payable and other current liabilities	3,692	1,131	1,520
Accrued taxes	(2,621)	8,863	(5,727)
Accrued interest and dividends	(94)	(294)	16
Other, net	2,110	417	(12,973)
Net cash provided by operating activities	80,154	88,055	47,197
Investing activities:			
Additions to utility plant (excludes allowance for funds used during construction)	(99,722)	(83,321)	(74,569)
Additions to real estate and other properties	(4,177)	(2,080)	(5,569)
Additions to equity investments	(4,784)	(15,859)	(63,042)
Acquisitions, net of cash received	—	—	(6,794)
Proceeds from New Mexico settlement	—	—	31,670
Investments in service contracts	—	—	(5,500)
Change in restricted cash	(13,914)	(7,378)	25,474
Net cash used in investing activities	(122,597)	(108,638)	(98,330)
Financing activities:			
Change in notes payable	18,475	(18,300)	49,725
Additional long-term debt	85,233	75,565	30,538
Reduction in preferred stock and long-term debt	(59,318)	(34,585)	(15,550)
Issuance of common stock	23,068	25,083	18,845
Dividends on common stock	(34,427)	(32,636)	(30,994)
Dividends on preferred and preference stock	(4,058)	(4,345)	(4,613)
Net contributions and advances for construction	12,935	9,386	7,614
Net cash provided by financing activities	41,908	20,168	55,565
Net (decrease) increase in cash and cash equivalents	(535)	(415)	4,432
Cash and cash equivalents at beginning of year	8,546	8,961	4,529
Cash and cash equivalents at end of year	$ 8,011	$ 8,546	$ 8,961

The accompanying notes are an integral part of these consolidated financial statements.

Statement of Consolidated Capitalization

DECEMBER 31, (THOUSANDS OF DOLLARS)	1998	1997
Common stock and retained earnings:		
Common stock, no par value—authorized 100,000,000 shares	$ 401,370	$ 373,927
Less treasury shares, at cost	(15,951)	(15,970)
Retained earnings	62,852	53,350
Cumulative translation adjustment	7,758	7,294
Total common stock and retained earnings	456,029	418,601
Cumulative preferred stock without mandatory redemption:		
United Water New Jersey, authorized 2,000,000 shares, stated value—$100 per share, issuable in series:		
4½% Series, authorized and outstanding 30,000 shares	3,000	3,000
4.55% Series, authorized and outstanding 60,000 shares	6,000	6,000
Total preferred stock without mandatory redemption	9,000	9,000
Cumulative preferred and preference stock with mandatory redemption, net of amount due within one year:		
United Water New Jersey:		
5% Series, authorized 15,000 shares; outstanding 6,000 and 6,600 shares	540	600
7⅜% Series, authorized and outstanding 150,000 shares	15,000	15,000
United Water New York:		
Authorized 100,000 shares, stated value—$100 per share issuable in series:		
$8.75 Series, issued and outstanding 22,000 and 24,000 shares	2,000	2,200
$9.84 Series, issued and outstanding 46,880 and 50,000 shares	4,375	4,688
United Water Idaho: 5%, authorized and outstanding 7,399 and 7,415 shares	607	605
United Water Resources:		
7⅝% Series B, authorized 300,000 shares; outstanding 285,000 and 300,000 shares	27,226	28,745
5% Series A, convertible preference, authorized 3,983,976 shares; outstanding 2,296,278 and 2,628,142 shares	30,534	34,741
Total preferred and preference stock with mandatory redemption	80,282	86,579
Long-term debt, net of amount due within one year:		
United Water New Jersey:		
First mortgage bonds, 5.8%-5.9%, due 2024 (weighted average 5.85%)	40,000	40,000
Unsecured promissory notes, variable rates, due 2025-2026 (weighted average 3.51% and 4.54%)	165,000	130,000
United Water New York:		
First mortgage bonds, 9⅜%, due 2001	600	900
Unsecured promissory notes, 5.65%-8.98%, due 2023-2025 (weighted average 6.74%)	51,000	51,000
United Water Resources:		
Promissory notes, 9.38%, due 2019	25,000	25,000
Promissory notes, floating LIBOR-based interest rate, due 2006	24,000	26,000
Promissory notes, 7.45%-7.9%, due 2007-2022 (weighted average 7.73%)	40,000	40,000
United Waterworks:		
Unsecured debt, 5.30%-10.05%, due 2000-2028 (weighted average 7.07% and 7.55%)	282,815	280,365
United Properties Group:		
Mortgage notes, 8%-10%, due 1999-2006 (weighted average 9.97% and 9.92%)	15,697	17,265
Floating rate LIBOR-based term loan, due 2000	7,211	7,251
New Jersey Wastewater Treatment Loans, 0%-4.2%, due 2013 (weighted average 2.48% and 2.22%)	1,646	1,931
United Water Mid-Atlantic: Promissory note at floating interest rate, due 2004	—	3,025
Total long-term debt	652,969	622,737
Total capitalization	$1,198,280	$1,136,917

The accompanying notes are an integral part of these consolidated financial statements.

One | Summary of Significant Accounting Policies

Principles of Consolidation: The consolidated financial statements include the accounts of United Water Resources (United Water, or the Company) and the subsidiaries in which it has more than 50% ownership. The Company accounts for investments in which it has significant influence under the equity method of accounting. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. Certain prior year amounts have been reclassified to conform with current year presentation.

Description of Business: United Water's principal utility subsidiaries include United Water New Jersey, United Water New York and United Waterworks. These subsidiaries provide water and wastewater services to approximately two million people in 13 states. Other significant wholly-owned subsidiaries of United Water include: United Properties Group (United Properties), which is engaged in real estate activities including commercial rentals, land development and sales, golf course operations, and consulting services; United Water UK, an equal partner with Lyonnaise Europe (a wholly-owned subsidiary of Suez Lyonnaise des Eaux) in the Northumbrian Partnership, which has acquired a 20% interest in Northumbrian Water Group plc (NWG), a major investor-owned water and wastewater company in the United Kingdom; and United Water Mid-Atlantic, which owns and operates water and wastewater systems. In addition, the Company has entered into public-private partnerships with the cities of Hoboken and Jersey City, New Jersey, whereby the municipalities retain ownership of their systems while the Company operates and maintains them. United Water also has several equity investments in the contract services business.

United Water's domestic utility subsidiaries are subject to regulation by the public utility commissions of the states in which they operate. Their accounting must comply with the applicable uniform system of accounts prescribed by these regulatory commissions and must also conform to generally accepted accounting principles as applied to rate-regulated public utilities. The Company continues to follow Statement of Financial Accounting Standards (SFAS) No. 71 "Accounting for the Effects of Certain Types of Regulation" for its regulated utilities. SFAS No. 71 provides for the recognition of regulatory assets and liabilities as allowed by state regulators that are considered probable of recovery.

Equity Investments: The Company holds an indirect investment in NWG and has representation on its board of directors, and owns a 50% stake in United Water Services and a 33.3% and 20.5% interest in United Water Services Canada (UWS Canada) and United Water Services Mexico (UWS Mexico), respectively. The Company accounts for these investments under the equity method of accounting by recording its proportionate share of earnings included in equity investments in the consolidated balance sheet and equity earnings of affiliates in the statement of consolidated income.

Foreign Currency Translation: Financial statements for United Water UK are translated into U.S. dollars at year-end exchange rates for assets and liabilities and weighted average exchange rates for income and expenses. The resulting cumulative translation adjustment is recorded as a separate component of stockholders' equity in the Company's statement of consolidated common equity.

Transactions for UWS Canada and UWS Mexico are recorded in U.S. dollars. Therefore, a foreign currency translation adjustment is not required for these entities.

Utility Plant: Utility plant is recorded at original cost, which includes direct and indirect labor and material costs associated with construction activities, related operating overheads and an allowance for funds used during construction (AFUDC). AFUDC is a non-cash credit to income and includes both the cost of borrowed funds and a return on equity funds attributable to plant under construction.

The original cost of utility property retired or otherwise disposed of in the normal course of business is charged to accumulated depreciation, and salvage (net of removal cost) is credited thereto; no gain or loss is recognized. The costs of property repairs, replacements and renewals of minor property items are included in maintenance expense when incurred.

Utility Plant Acquisition Adjustments: Utility plant acquisition adjustments represent the difference between the purchase price and the book value of net assets acquired, and are amortized, generally, on a straight-line basis over a 40-year period. Utility plant acquisition adjustments include a premium paid to acquire operating utilities. At each balance sheet date, the Company evaluates the realizability of utility plant acquisition adjustments on the basis of expected future undiscounted cash flows. Based on its most recent evaluation, the Company believes that no impairment of utility plant acquisition adjustments exists at December 31, 1998.

Advances and Contributions in Aid of Construction: When required by the public utility commissions of the states in which the Company's utility subsidiaries operate, outside parties, generally customers and developers, make payments to the Company to fund certain utility capital expenditures to provide water or wastewater service to new customers. Non-refundable amounts received by the Company are recorded as contributions in aid of construction, except where the Company is required to record such amounts directly as a reduction to utility plant. Refundable amounts received are recorded as advances, and are refundable, for limited periods of time, generally as new customers begin to receive service. The remaining balance of any advances received, after the Company has made all required refunds of such advances, is transferred to contributions in aid of construction.

The balances of advances and contributions are used to reduce utility plant in determining rate base, and plant funded by advances and contributions is generally not depreciated. However, the public utility commissions in several of the states in which the Company operates permit the depreciation of plant funded by contributions in aid of construction, but also require that contributions be amortized, so that there is no net effect on income from the depreciation of the contributed plant. For income tax purposes, advances and contributions received after 1986 and through June 1996 are included as taxable income, and the related plant is depreciated for tax purposes. In accordance with changes in the tax law, effective June 12, 1996, advances and contributions are no longer included in taxable income, nor is the related plant depreciated for tax purposes.

Jointly Owned Facilities: Utility plant includes United Water New Jersey's 50% interest in the Wanaque South Water Supply Project, the net book value of which was $42 million and $42.8 million at December 31, 1998 and 1997, respectively. United Water New Jersey's share of the project's operating expenses is included in operation and maintenance expenses.

Regulatory Assets: Included in deferred charges and other assets are regulatory items that are expected to be recognized when included in future rates and recovered from customers as directed by the state public utility commissions. These regulatory assets include items that the public utility commissions have ordered the Company's regulated utilities to defer and prudently incurred costs where the Company expects that recovery is probable because of the past practices of the public utility commissions.

Regulatory assets consisted of the following at December 31:

(THOUSANDS OF DOLLARS)	1998	1997
Recoverable income taxes	$39,328	$39,818
Deferred employee benefits	20,918	22,918
Rate case	3,308	2,459
Tank painting	3,117	3,181
Other	9,877	11,372
Total regulatory assets	$76,548	$79,748

Real Estate: Real estate properties are carried at the lower of cost, which includes original purchase price and direct development costs, discounted cash flow value or fair value. Real estate taxes and interest costs are capitalized during the development period. The amount of interest capitalized was $650,890 in 1998, $651,251 in 1997 and $620,000 in 1996. Real estate operating revenues include rental income from commercial properties, proceeds from the disposition of real estate properties, revenues from golf course operations and fees from consulting services.

Unamortized Debt Expense: Debt premium, debt discount and deferred debt expenses are amortized to income or expense over the lives of the applicable issues.

Revenues From Utility Operations: United Water New Jersey and United Waterworks recognize as revenues billings to customers, plus estimated revenues for consumption for the period from the date of the last billing to the balance sheet date. United Water New York recognizes revenues as bills are rendered to customers and does not accrue for unbilled revenues. United Water New York and United Water New Rochelle have been directed by the New York Public Service Commission to institute a Revenue Reconciliation Clause, which requires the reconciliation of billed revenues with pro forma revenues that were used to set rates. Any variances outside a threshold range are accrued or deferred for subsequent recovery from or refund to customers. At December 31, 1998 and 1997, United Water New York and United Water New Rochelle had $4.4 million and $3.6 million, respectively, of net unamortized revenue accruals, resulting from revenues which were less than the amounts used to set rates. These amounts are expected to be recovered over a three-year period.

Revenues From Real Estate Activities: Revenues from real estate sales are recognized when the transaction is consummated and title has passed. Revenues from real estate transactions were $4.9 million, $11.2 million and $5.4 million in 1998, 1997 and 1996, respectively.

United Properties owns several office buildings, with an aggregate net book value of $57.7 million (net of accumulated depreciation of $11 million) at December 31, 1998, which are leased to tenants under various operating leases. The following is a schedule, by year, of the minimum future rental income on non-cancelable operating leases outstanding at December 31, 1998:

(THOUSANDS OF DOLLARS)	
1999	$ 5,827
2000	6,408
2001	6,359
2002	6,251
2003	5,532
Thereafter	22,901
Total minimum future rental income	$53,278

Revenues From Public-Private Partnerships: In May 1996, United Water entered into a five-year contract with Jersey City to operate its municipal water system. This contract stipulates that the city can terminate the contract in the fourth and fifth years, subject to a termination penalty. If the city terminated the contract, this would not have a material effect on United Water's financial position or results of operations. The contract also provides for monthly service fees which are recorded as revenues when billed. In addition, certain incentives based on collection and marketing goals are recognized when earned. Service fee revenues for the years ended December 31, 1998 and 1997 and for the eight months ended December 31, 1996 were $10 million, $9.2 million and $4.7 million, respectively.

In 1994, the Company entered into a ten-year contract with the city of Hoboken to operate, maintain and manage its municipal water system. In 1996, this contract was extended for an additional ten years. Under this contract, revenues are recorded monthly based upon customer billings. Revenues for the years ended December 31, 1998, 1997 and 1996 were $4 million, $3.9 million and $3.5 million, respectively.

Depreciation: Depreciation of utility plant and real estate properties is recognized using the straight-line method over the estimated service lives of the properties. Utility plant depreciation rates are prescribed by the public utility commissions. The provisions for depreciation in 1998, 1997 and 1996 were equivalent to 2.4%, 2.3% and 2.1%, respectively, of average depreciable utility plant in service. Real estate properties are depreciated over estimated lives ranging between 25 and 50 years. For federal income tax purposes, depreciation is computed using accelerated methods and, in general, shorter depreciable lives as permitted under the Internal Revenue Code.

Income Taxes: The Company and its eligible subsidiaries file a consolidated federal income tax return. Federal income taxes are deferred under the liability method in accordance with SFAS No. 109, "Accounting for Income Taxes." Under the liability method, deferred income taxes are provided for all differences between financial statement and tax basis of assets and liabilities. Additional deferred income taxes and offsetting regulatory assets or liabilities are recorded to recognize that income taxes will be recoverable or refundable through future revenues.

Investment tax credits arising from property additions are deferred and amortized over the estimated service lives of the related properties.

Statement of Cash Flows: United Water considers all highly liquid investments with original maturities of three months or less to be cash equivalents. The Company made cash payments for interest (net of amounts capitalized) and federal and state income taxes as follows:

(THOUSANDS OF DOLLARS)	1998	1997	1996
Interest, net of amounts capitalized	$44,651	$44,400	$43,728
Income taxes	11,520	7,413	11,921

The following is a supplemental schedule of non-cash transactions in 1998 and 1997:

(THOUSANDS OF DOLLARS)	1998	1997
Cumulative translation adjustment	$ 464	$ 591
Conversion of 5% preference stock	4,576	4,967

Two I Equity Investments

On June 28, 1996, United Water and Lyonnaise Europe formed the Northumbrian Partnership (the Partnership), an equal partnership which has acquired a 20% interest in NWG, a major investor-owned water and wastewater company in the United Kingdom. United Water's initial $62 million investment in the Partnership was made through its wholly-owned subsidiary in the United Kingdom, United Water UK Limited. Investment in the Partnership was $96.3 million and $78.7 million at December 31, 1998 and 1997, respectively, and is included in equity investments in the consolidated balance sheet. United Water's share of the Partnership's earnings, which totaled $17.1 million and $13.6 million (excluding the windfall profits tax) in 1998 and 1997, respectively, is included in equity earnings of affiliates in the accompanying statement of consolidated income.

During 1997, the United Kingdom's new Labor Government imposed a one-time "windfall profits" tax on privatized utilities. The levying of this one-time tax negatively impacted the Company's earnings from its investment in NWG by $13.1 million, which was partially offset by the effect of a change in the tax rate on deferred taxes of $2.8 million. The result was a net impact of $10.3 million. The imposition of this tax had been factored into the Company's financial analysis at the time of its investment in NWG and was considered in determining the purchase price. The tax did not have an effect on United Water's cash flow or ability to pay dividends, nor did it affect the long-term benefit the Company expected to derive from its investment in NWG.

On July 28, 1997, United Water Services, a 50/50 joint venture between United Water and Suez Lyonnaise des Eaux acquired the remaining 50% stake in JMM Operational Services.

United Water Services provides contract operations and maintenance services for water and wastewater facilities and is pursuing additional contract operations. As a result, United Water Services was awarded several contracts. The largest awards include a ten-year contract to operate the wastewater systems in Milwaukee, Wisconsin, and a 20-year contract to operate the water system in Atlanta, Georgia, with a minority partner. United Water Services also operates a meter installation subsidiary, United Metering, which it purchased from United Water in December 1997 for book value of $6.2 million.

In July 1997, the Company also acquired a 30% and a 20% interest in UWS Canada and UWS Mexico, respectively. In December 1998, United Water purchased additional interests and now has a 33.3% and a 20.5% interest in UWS Canada and UWS Mexico, respectively.

At December 31, 1998 and 1997, United Water had equity investments, relating to contract services, of approximately $19.8 million and $20.2 million, respectively, including investments in Canada and Mexico. This amount is included in equity investments in the accompanying consolidated balance sheet. United Water's share of earnings in these investments is included in equity earnings of affiliates in the accompanying statement of consolidated income.

Three I New Mexico Settlement

On March 29, 1996, the Company settled the condemnation proceeding with the city of Rio Rancho, New Mexico (the City). The agreement was approved on the same day by the Thirteenth Judicial District Court in New Mexico. Under the terms of the agreement, the Company agreed to accept $67 million for the water and wastewater systems of its United Water New Mexico operations. Results of this transaction are included in the Company's first quarter 1996 earnings.

Four | Notes Payable

United Water and its subsidiaries have a number of credit lines with banks. Borrowings under these credit lines generally bear interest at rates between the London Interbank Offered Rate (LIBOR) and the prime lending rate. United Water pays commitment fees under arrangements with certain of these banks to compensate them for services and to support these lines of credit. There are no legal restrictions placed on the withdrawal or other use of these bank balances.

The total credit lines available, the amounts utilized and the weighted average interest rates at December 31 were as follows:

(THOUSANDS OF DOLLARS)	1998	1997
Total credit lines available	$280,500	$235,800
Utilized:		
Drawn	93,400	74,925
Pledged	655	3,055
Weighted average interest rates	5.5%	5.9%

Five | Long-Term Debt

The long-term debt repayments over each of the next five years are as follows: 1999—$3.7 million; 2000—$12.2 million; 2001—$19.7 million; 2002—$4.7 million and 2003—$4.8 million. United Water New Jersey, United Water New York, United Waterworks and other subsidiaries of United Water are subject to certain restrictive covenants related to their issued debt.

In June 1997, United Water issued $40 million of 7.45%-7.9% Senior Notes ($15 million due 2007 and $25 million due 2022). Proceeds from the notes were used to refinance existing short-term debt of the Company.

In August 1997, United Waterworks issued $20 million of 5.3% tax-exempt Water Resource Development Revenue Bonds, due 2027, through the Idaho Water Resource Board. The proceeds are being used to finance a portion of the costs of certain facilities to be owned by United Water Idaho (a subsidiary of United Waterworks).

In December 1994, United Waterworks entered into a medium-term note program that enabled United Waterworks to issue up to $75 million of debt with terms ranging from 9 months to 30 years. The interest rates are set as notes are issued under the program. The first $10 million of notes under this program were issued in 1995. In October 1997, United Waterworks issued $15 million of notes under this program, at a rate of 6.8%, with the full amount maturing in 2007. In February 1998, United Waterworks issued an additional $40 million of notes under this program ($20 million at 6.97% due 2023, $15 million at 7.1% due 2028 and $5 million at 6.9% due 2017). In November 1998, United Waterworks issued the final $10 million of notes under this program ($5 million at 6.44% due 2008 and $5 million at 6.97% due 2023). The proceeds were used to redeem outstanding notes payable.

In June 1996, United Water entered into a $30 million long-term note agreement with Credit Lyonnais to partially fund its investment in the Northumbrian Partnership. The loan bears interest at a LIBOR-based floating rate and is payable in annual installments through June 2006. In December 1998, the Company entered into an interest rate swap agreement which fixed the interest rate at 5.24% for 1999 and 5.34% for the years 2000 through 2003.

In December 1998, United Water New Jersey issued $35 million of 5% Water Facilities Revenue Bonds through the New Jersey Economic Development Authority due 2028. The proceeds are being used to finance the cost of acquiring, constructing and reconstructing certain water transmission, transportation, storage, treatment, and distribution facilities located in Passaic, Bergen, Sussex, and Hudson counties in New Jersey.

In January 1999, United Water issued $30 million of Senior Notes ($5 million at 6.07% due 2005, $10 million at 6.43% due 2009, $10 million at 6.7% due 2019 and $5 million at 7.04% due 2019). The proceeds were used to redeem all remaining shares of 7⅝% Series B cumulative preferred stock. See Note 7 to the consolidated financial statements for further details.

Six | Commitments and Contingencies

Capital Expenditures

The future capital expenditures of the Company's utility subsidiaries are projected to aggregate $262 million over the next five years, including $57 million and $58 million in 1999 and 2000, respectively. United Properties currently projects spending $25.9 million over the next five years for capital expenditures on its existing real estate portfolio, including $8.3 million and $6.9 million in 1999 and 2000, respectively.

Operating Leases

United Water's total consolidated rental expense was approximately $6.5 million in 1998, $6.2 million in 1997 and $5.1 million in 1996. The minimum future lease payments under all non-cancelable operating leases, which consist primarily of buildings and automobiles, at December 31, 1998 are as follows:

(THOUSANDS OF DOLLARS)	
1999	$ 4,828
2000	3,576
2001	2,106
2002	1,137
2003	480
Thereafter	1,840
Total minimum future lease payments	$13,967

Legal Matters

United Water has been notified that it may be one of several defendants in a lawsuit involving cancer incidences in Dover Township, New Jersey. A complaint has not been filed; however, an agreement was signed on January 29, 1998 with the potential plaintiffs that would toll the statute of limitations for a time period of at least eighteen months. Management believes if a lawsuit is commenced, the Company will have meritorious defenses, and there will be a number of parties against whom it will have recourse. Therefore, the Company believes that the ultimate disposition of this matter will not have a material adverse effect on the financial position or results of operations.

The Company has various purchase commitments for materials, supplies and other services incidental to the ordinary conduct of business. In addition, the Company is routinely involved in legal actions arising in the ordinary course of its utility operations. In the opinion of management, none of these matters will have a material adverse impact on the Company.

Seven | Preferred and Preference Stock

The utility subsidiaries of the Company have issued and outstanding cumulative preferred stock, generally with mandatory redemption provisions requiring annual sinking fund payments. These sinking fund requirements total $2,073,000 in each of the years 1999 and 2000 and $4,216,000 in 2001 through 2003. The redemption of cumulative preferred stock was $2,073,000 in 1998 and $260,000 in each of the years 1997 and 1996. In addition, except as described in the next paragraph, optional sinking fund provisions can be exercised and redemptions made at specific prices for all preferred stock issues. Redemptions require payment of accrued and unpaid dividends up to the date fixed for redemption.

As a result of the merger with GWC Corporation in 1994, United Water issued 3,341,078 shares ($46 million par value) of 5% Series A cumulative convertible preference stock, valued at $43.3 million at the time of the merger and $30 million of 7⅝% Series B cumulative preferred stock, valued at $31.1 million at the time of the merger. Lyonnaise American Holding, Inc.(LAH) owned 97.7% of the Series A preference stock outstanding. The Series B preferred stock has a $1.5 million mandatory annual redemption commencing in 1998. Shares of the Series B preferred stock could not be redeemed by the Company prior to September 1, 1997. Each share of the Series A preference stock outstanding may be converted into .83333 shares of United Water common stock at any time commencing April 22, 1996. However, under the Governance Agreement between United Water and LAH, LAH may convert no more than 10% of the Series A preference stock it owns during the year commencing April 22, 1996, and an additional 10% cumulatively per year thereafter until April 22, 2003, at which time these conversion restrictions end. During 1998, 331,864 shares of the Series A preference stock with a value of $4.6 million were converted into 276,543 shares of United Water common stock with a value of $4.4 million. During 1997, 360,014 shares of the Series A preference stock with a value of $5 million were converted into 299,958 shares of United Water common stock with a value of $4.7 million. As a result, at December 31, 1998, LAH owned approximately 29.5% of the issued and outstanding United Water common stock and approximately 98.1% of the issued and outstanding United Water 5% cumulative convertible preference stock. United Water may not redeem any of the outstanding, unconverted Series A preference stock prior to maturity on April 22, 2004.

On December 8, 1998, the Company called for redemption of the remaining 285,000 shares of its 7⅝% Series B cumulative preferred stock. The redemption, which occurred on January 8, 1999, resulted in the payment of principal, accrued dividends and premium totaling $30 million, with $1.3 million relating to the premium paid on the early redemption. The preferred stock was redeemed with $30 million of 6.07%-7.04% Senior Notes due 2005-2019.

Eight | Incentive Stock Plans

Under the Company's management incentive plan, the following options have been granted to key employees:

	NUMBER OF OPTIONS	WEIGHTED AVERAGE EXERCISE PRICE PER OPTION
Outstanding at December 31, 1995	814,670	$14.508
Granted	204,300	12.250
Exercised	(120,813)	12.965
Canceled or expired	(10,340)	14.703
Outstanding at December 31, 1996	887,817	$14.196
Granted	370,840	15.580
Exercised	(439,605)	15.032
Canceled or expired	(20,062)	15.501
Outstanding at December 31, 1997	798,990	$14.345
Granted	408,480	18.625
Exercised	(186,808)	15.182
Canceled or expired	(23,380)	18.626
Outstanding at December 31, 1998	997,282	$15.841

All options are currently exercisable and represent the only stock options outstanding at December 31, 1998. A total of 2,026,175 common shares are reserved for issuance under the management incentive plan.

In May 1993, the shareholders approved the creation of dividend units to be issued in conjunction with stock options granted under the management incentive plan. One dividend unit may be attached to each unexercised option to purchase a share of United Water common stock, which entitles the option holder to accrue, as a credit against the option exercise price, the aggregate dividends actually paid on a share of United Water common stock while the dividend unit is in effect. In May 1997, the shareholders amended the plan to provide that the dividend units be granted separately and detached from the stock options and accrue dividends for a predetermined period of time, after which, they are distributed. United Water recorded compensation expense of $2.6 million in 1998, $2.3 million in 1997 and $2.5 million in 1996 with respect to the management incentive plan.

In October 1995, the Financial Accounting Standards Board (FASB) issued SFAS No. 123, "Accounting for Stock-Based Compensation," which establishes financial accounting and reporting standards for stock-based employee compensation plans. The statement defines a fair value based method of accounting for employee stock options and similar equity instruments and encourages the use of that method of accounting for all employee stock compensation plans. However, SFAS No. 123 also permits the measurement of compensation costs using the intrinsic value based method of accounting prescribed by Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees." The Company has elected to account for its employee stock compensation plans under the guidance prescribed by APB Opinion No. 25 and has made the required pro forma disclosures of net income and earnings per share as if the fair value based method of accounting defined in SFAS No. 123 had been applied as indicated below:

(THOUSANDS OF DOLLARS EXCEPT PER SHARE DATA)	1998	1997	1996
Net income:			
As reported	$43,929	$29,331	$34,010
Pro forma	44,140	29,273	34,079
Earnings per common share:			
As reported	$ 1.19	$ .83	$ 1.01
Pro forma	1.19	.83	1.01
Earnings per common share—assuming dilution:			
As reported	$ 1.17	$ .83	$ 1.00
Pro forma	1.17	.83	1.01

The fair value for these options was estimated at the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions for the years ended December 31, 1998, 1997 and 1996, respectively: expected volatility of 21.1%, 20.3% and 21.5%; risk-free interest rates of 5.5%, 6.4% and 5.5%; expected life of 6 years and dividend yields of 5.0% in 1998, 5.9% in 1997 and 0.0% in 1996. The weighted average fair value of each option granted during the years ended December 31, 1998, 1997 and 1996 was $2.99, $2.30 and $4.30, respectively. The Black-Scholes option-pricing model requires the input of highly subjective assumptions including the expected stock price volatility. Changes in the subjective input assumptions can materially affect the fair value estimate. In management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

In May 1988, the shareholders approved a restricted stock plan for certain key employees. United Water issued 1,250 shares in 1996 in connection with the restricted stock plan. Such shares are earned by the recipients over a five-year period. United Water recorded compensation expense of $69,000 in 1996 with respect to this restricted stock plan.

Nine | Shareholder Rights Plan

In July 1989, the board of directors of United Water approved a Shareholder Rights Plan designed to protect shareholders against unfair and unequal treatment in the event of a proposed takeover. It also guards against partial tender offers and other hostile tactics to gain control of United Water without paying all shareholders a fair price. Under the plan, each share of United Water's common stock also represents one Series A Participating Preferred Stock Purchase Right (Right) until the Rights become exercisable. The Rights attach to all of United Water's common stock outstanding as of August 1, 1989, or subsequently issued, and expire on August 1, 1999.

The Rights would be exercisable only if a person or group acquired 20% or more of United Water's common stock or announced a tender offer that would lead to ownership by a person or group of 20% or more of the common stock.

In certain cases where an acquirer purchased more than 20% of United Water's common stock, the Rights would allow shareholders (other than the acquirer) to purchase shares of United Water's common stock at 50% of market price, diminishing the value of the acquirer's shares and diluting the acquirer's equity position in United Water. If United Water were acquired in a merger or other business combination transaction, under certain circumstances the Rights could be used to purchase shares in the acquirer at 50% of the market price. Subject to certain conditions, if a person or group acquired 20% or more of United Water's common stock, United Water's board of directors may exchange each Right held by shareholders (other than the acquirer) for one share of common stock or 1/100 of a share of Series A Participating Preferred Stock. If an acquirer successfully purchased 80% of United Water's common stock after tendering for all of the stock, the Rights would not operate. If holders of a majority of the shares of United Water's common stock approved a proposed acquisition under specified circumstances, the Rights would be redeemed at one cent each. They could also be redeemed by United Water's board of directors for one cent each at any time prior to the acquisition of 20% of the common stock by an acquirer.

On September 15, 1993, United Water's Shareholder Rights Plan was amended in connection with United Water's execution of a merger agreement with GWC Corporation. The amendment generally excepts the majority stockholder of United Water (Suez Lyonnaise des Eaux) and its affiliates and associates from triggering the Rights through the execution of the merger agreement, the performance of the transactions contemplated therein or otherwise.

Ten | Employee Benefits

In February 1998, the FASB issued SFAS No. 132, "Employers' Disclosures about Pensions and Other Postretirement Benefits". This statement addresses disclosure only. It does not address measurement or recognition. United Water adopted SFAS No. 132 in 1998.

Defined Benefit Pension Plans: Most of United Water's employees are covered by trusteed, non-contributory, defined benefit pension plans. Benefits under these plans are based upon years of service and the employee's compensation during the last five years of employment. United Water's policy is to fund amounts accrued for pension expense to the extent deductible for federal income tax purposes. It is expected that no funding will be made for 1998.

Postretirement Benefit Plans Other Than Pensions: The Company sponsors a defined benefit postretirement plan that covers hospitalization, major medical benefits and life insurance benefits for retired salaried and non-salaried employees. The Company is funding a portion of its postretirement health care benefits through contributions to Voluntary Employees' Beneficiary Association (VEBA) Trusts.

The following sets forth the qualified plans' funded status and reconciles that funded status to the amounts recognized in the Company's balance sheet as of December 31:

Pension

(THOUSANDS OF DOLLARS)	1998	1997
Change in benefit obligation		
Benefit obligation at beginning of year	$138,092	$124,342
Service cost	4,367	3,553
Interest cost	9,971	9,439
Actuarial loss	5,119	7,492
Benefits paid	(6,970)	(6,734)
Benefit obligation at end of year	150,579	138,092
Change in plan assets		
Fair value of plan assets at beginning of year	200,853	174,560
Actual return on plan assets	33,118	33,027
Benefits paid	(6,970)	(6,734)
Fair value of plan assets at end of year *	227,001	200,853
Funded status	76,422	62,761
Unrecognized transition obligation	(3,569)	(4,196)
Unrecognized actuarial gain	(45,483)	(39,154)
Unrecognized prior service cost	1,867	2,015
Prepaid benefit cost	$ 29,237	$ 21,426

* Primarily stocks and bonds, including $13.7 million and $11.2 million, respectively, in common stock of United Water.

Other Benefits

(THOUSANDS OF DOLLARS)	1998	1997
Change in benefit obligation		
Benefit obligation at beginning of year	$ 51,900	$ 42,903
Service cost	2,953	2,091
Interest cost	3,954	3,299
Actuarial loss	2,620	5,312
Benefits paid	(1,044)	(1,705)
Benefit obligation at end of year	60,383	51,900
Change in plan assets		
Fair value of plan assets at beginning of year	21,704	16,695
Actual return on plan assets	4,207	3,562
Employer contribution	2,223	3,152
Benefits paid	(1,044)	(1,705)
Fair value of plan assets at end of year	27,090	21,704
Funded status	(33,293)	(30,196)
Unrecognized transition obligation	20,470	21,911
Unrecognized actuarial gain	(7,419)	(7,818)
Accrued benefit cost	$(20,242)	$(16,103)

The components of net periodic pension income for the Company's qualified and supplemental plans were as follows:

(THOUSANDS OF DOLLARS)	1998	1997	1996
Service cost	$ 4,600	$ 3,726	$ 3,945
Interest cost	10,438	9,842	9,379
Expected return on plan assets	(19,748)	(16,275)	(14,950)
Amortization of transition obligation	(583)	(583)	(543)
Amortization of gain	(1,941)	(1,549)	(967)
Amortization of prior service cost	226	268	400
Net periodic pension income	$ (7,008)	$ (4,571)	$ (2,736)

Assumptions as of December 31:

	1998	1997	1996
Assumed discount rate	7.125%	7.375%	7.75%
Expected return on assets	10.0%	9.5%	9.5%
Range of compensation increase	3.75-4.5%	3.75-4.5%	3.75-4.5%

Net periodic postretirement benefit cost components were as follows:

(THOUSANDS OF DOLLARS)	1998	1997	1996
Service cost	$ 2,953	$ 2,091	$ 2,404
Interest cost	3,954	3,299	3,095
Expected return on plan assets	(1,896)	(1,396)	(1,098)
Amortization of transition obligation	1,441	1,441	1,441
Amortization of gain	(90)	(462)	(114)
Net periodic benefit cost	$ 6,362	$ 4,973	$ 5,728

Assumptions as of December 31:

	1998	1997	1996
Assumed discount rate	7.375%	7.625%	8.0%
Expected return on assets	9.5%	9.5%	9.5%

The associated health care cost trend rate used in measuring the postretirement benefit obligation at December 31, 1998 was 7.1%, gradually declining to 5.5% in 2002 and thereafter. Changing the assumed health care cost trend rate by one percentage point in each year results in changes in service cost and interest, and plan obligation as follows:

(IN MILLIONS)	1-PERCENTAGE POINT INCREASE	1-PERCENTAGE POINT DECREASE
Effect on total service and interest cost components	$1.5	$(1.1)
Effect on postretirement benefit obligation	9.6	(7.7)

Postretirement health care costs in excess of those currently included in rates have been deferred in those jurisdictions where their recovery is deemed probable. At December 31, 1998 and 1997, United Water had regulatory assets relating to deferred employee benefits of $20.9 million and $22.9 million, respectively, for recovery in future rates.

Supplemental Benefit Plans: Certain categories of employees are covered by non-funded supplemental plans. The projected benefit obligations of these plans at December 31, 1998 and 1997 totaled $6.5 million and $6.2 million, respectively. At December 31, 1998 and 1997, the unfunded accumulated benefit obligations of $6 million and $5.9 million, respectively, have been recorded in other deferred credits and liabilities and intangible pension assets of $372,000 and $678,000, respectively, are included in deferred charges and other assets.

United Water maintains defined contribution savings plans which permit employees to make voluntary contributions with Company matching as defined by the plan agreements. United Water made contributions of $1,764,000, $1,155,000 and $1,167,000 in 1998, 1997 and 1996, respectively, to defined contribution savings plans.

Eleven | Rate Matters

The following rate decisions were rendered to United Water's regulated utilities during 1998:

(THOUSANDS OF DOLLARS)	EFFECTIVE DATE	ALLOWED ROE	ANNUAL INCREASE	% INCREASE
Pennsylvania	2/03/98	11.00	$2,140	11.0
Pennsylvania–DSIC*	4/01/98	—	32	0.2
Delaware (1998 case)	5/11/98	N/A	2,385[a]	14.4
Pennsylvania–STAS**	6/01/98	—	(23)[b]	0.1
Pennsylvania–DSIC*	7/01/98	—	41	0.2
Idaho	7/06/98	10.75	1,916	8.7
Indiana (4 rate cases)	7/08/98	10.50	1,041	18.3
New York (Sloatsburg/Pothat)	7/18/98	—	29	8.8
New Rochelle (Purchased Water)	8/24/98	—	453[c]	2.6
Pennsylvania–DSIC*	10/01/98	—	30	0.2
New Rochelle (Revenue Rec.)	11/01/98	—	81[d]	0.5
New Rochelle (3rd Stage)	11/19/98	—	491[e]	2.8
Owego	1/01/99	10.00	21	2.3
Pennsylvania–DSIC*	1/01/99	—	54	0.3
Totals			$8,691	

* Distribution System Improvement Charge
** State Tax Adjustment Surcharge
[a] Interim increase, granted subject to refund. Decision pending.
[b] Reduction on the Capital Stock and Franchise Tax.
[c] Pass-through for purchased water expense increase.
[d] One-third of a three-year recovery.
[e] Third-stage increase of a three-year settlement.

At December 31, 1998, the most significant rate cases pending were filed by United Water Florida and United Water Delaware. The increases were requested primarily to fund capital investments and meet higher operation and maintenance costs. In May 1998, United Water Florida applied for rate relief in the amount of $2.2 million, or 24.3%, in water revenues and $3.1 million, or 18.7%, in wastewater revenues.

In March 1998, United Water Delaware applied for rate relief in the amount of $4.1 million, or 24.8%, in water revenues. On May 11, 1998, United Water Delaware placed $2.4 million in increased revenues in effect, subject to refund. Management believes that any potential refunds will not have a material effect on earnings.

On October 26, 1996, United Water Delaware placed $2.3 million in increased revenues in effect, subject to refund. On July 15, 1997, the Delaware Public Utility Commission granted the Company a permanent rate increase of $1.6 million. On July 16, 1997, the Company filed an appeal and application for a stay of the Commission's Order. On July 29, 1997, the Delaware Superior Court granted a stay of the Commission decision pending the appeal. On March 31, 1998, the Superior Court decided in favor of the Commission. The Company appealed this decision to the Supreme Court of Delaware and on February 11, 1999, the Supreme Court reversed the Commission's decision which denied the $.7 million annual revenue increase, subject to refund and remanded the matter to the Commission.

The Company expects that the Commission will enter an Order on remand which will eliminate the prospect of refunding any part of the $2.3 million.

The Company has requested and received recovery of its regulatory assets for postretirement benefits other than pension as well as the recognition of the current expense for these benefits for the majority of its regulated subsidiaries. The regulatory assets are expected to be recovered over an average period of 15 years. At December 31, 1998, three regulated subsidiaries were awaiting decisions from the applicable commissions. Management believes it will receive favorable decisions on the pending cases prior to the end of 1999.

Generally, the rate awards the Company's operating utilities actually receive are less than the amounts requested, primarily due to differing positions of the parties involved and/or updated information provided during the proceedings.

Twelve I Income Taxes

Deferred Income Tax Assets and Liabilities: Deferred tax liabilities (assets) and deferred investment tax credits consisted of the following at December 31:

(THOUSANDS OF DOLLARS)	1998	1997
Basis differences of property, plant and equipment	$140,094	$130,891
Real estate transactions and capitalized costs	15,726	15,586
Prepaid employee benefits	10,941	8,550
Other liabilities	24,151	23,052
Gross deferred tax liabilities	190,912	178,079
Alternative minimum tax credit carryforwards	(12,754)	(11,223)
Other assets	(4,763)	(5,862)
Gross deferred tax assets	(17,517)	(17,085)
Deferred investment tax credits	21,973	22,496
Total deferred income taxes and investment tax credits	$195,368	$183,490

Income Tax Provision: A reconciliation of income tax expense at the statutory federal income tax rate to the actual income tax expense for 1998, 1997 and 1996 is as follows:

(THOUSANDS OF DOLLARS)	1998	1997	1996
Statutory tax rate	35%	35%	35%
Federal taxes at statutory rates on pretax income before preferred stock dividends of subsidiaries	$24,389	$19,779	$22,544
Utility plant acquisition adjustment	733	641	1,725
State income taxes, net of federal benefit	985	835	1,823
Deferred investment tax credits	(523)	(510)	(499)
Equity in foreign investments	(5,985)	(1,135)	(2,476)
Other	(149)	969	394
Provision for income taxes	$19,450	$20,579	$23,511

Income tax expense for 1998, 1997 and 1996 consisted of the following:

(THOUSANDS OF DOLLARS)	1998	1997	1996
Current:			
Federal	$ 7,146	$10,668	$ 5,919
State	1,349	969	1,310
Total current	$ 8,495	$11,637	$ 7,229
Deferred (prepaid):			
Accelerated depreciation	$ 8,305	$ 7,437	$ 7,612
Contributions and advances for construction	401	200	(1,855)
Prepaid employee benefits	2,391	1,400	1,931
UWNJ debt refinancing	—	—	3,053
Real estate transactions and capitalized costs	117	(181)	64
Alternative minimum tax	(1,531)	(1,507)	(741)
Investment tax credits	(523)	(510)	(499)
State income taxes, net of federal benefit	192	316	972
Transfer of New Mexico operations	—	—	5,365
Other	1,603	1,787	380
Total deferred	$10,955	$ 8,942	$16,282
Total provision for income taxes	$19,450	$20,579	$23,511

The Company considers the undistributed earnings of United Water UK to be permanently reinvested and has not provided deferred taxes on these earnings. At December 31, 1998 and 1997, cumulative undistributed earnings were $18.8 million and $5.4 million, respectively. These undistributed earnings could become subject to additional tax if remitted, or deemed remitted, as a dividend. Management believes it is not practicable to determine the amount of the unrecognized deferred tax liability.

Thirteen I Fair Value of Financial Instruments

The carrying amounts at December 31, 1998 and 1997, of those current assets and liabilities that are considered financial instruments approximates their fair values at those dates because of the short maturity of those instruments. Such current assets and liabilities include cash and cash equivalents, restricted cash, accounts receivable and unbilled revenues, notes payable, accounts payable and other current liabilities, and accrued interest and dividends. Real estate and other investments consist primarily of real estate and equity investments in affiliates and are not financial instruments. The Company understands that there are no quoted market prices for the Company's preferred stock, preference stock or long-term debt. The fair values of the Company's long-term debt and preferred and preference stock have been determined by discounting their future cash flows using approximate current market interest rates for securities of a similar nature and duration.

The estimated fair values of United Water's financial instruments at December 31 were as follows:

(THOUSANDS OF DOLLARS)	CARRYING AMOUNT	FAIR VALUE
1998		
Long-term debt	$652,969	$715,993
Preferred and preference stock with mandatory redemption	80,282	87,601
1997		
Long-term debt	$622,737	$673,321
Preferred and preference stock with mandatory redemption	86,579	96,425

The Company's customer advances for construction have a carrying value of $30.6 million and $27.4 million at December 31, 1998 and 1997, respectively. Their relative fair values cannot be accurately estimated since future refund payments depend on several variables, including new customer connections, customer consumption levels and future rate increases. The Company holds an interest rate cap to limit its exposure to a maximum interest rate of 7% on the United Water New Jersey Variable Rate Demand Water Facilities Refunding Bonds aggregating $130 million. In addition, United Water entered into an interest rate swap agreement on the $30 million long-term note agreement with Credit Lyonnais which fixed the interest rate at 5.24% for 1999 and 5.34% for the years 2000 through 2003. The fair values and carrying amounts of these financial instruments were not material at December 31, 1998.

Fourteen | Discontinued Operations

In December 1996, the Company announced its intention to dispose of its environmental testing business, closing its Laboratory Resources' operation in Teterboro, New Jersey. Subsequently, in January 1997, it sold its laboratory facility in Brooklyn, Connecticut. The subsidiary had been operating in a very competitive environment over a prolonged period of time and had not contributed to the Company's earnings, with a net loss of $1.5 million in 1996. The Company recorded an estimated provision of $1.1 million, net of income taxes, for severance, future lease obligations and other related costs, included in the loss on disposal of discontinued business in the accompanying statement of consolidated income. The operating results of Laboratory Resources prior to the date of discontinuance are shown separately in the accompanying statement of consolidated income and all of the financial statements of prior periods have been restated to reflect the discontinuance of Laboratory Resources' operations.

Fifteen | Earnings Per Share

In February 1997, the FASB issued SFAS No. 128, "Earnings per Share" (EPS), which specifies the computation, presentation and disclosure requirements for earnings per share for entities with publicly held common stock or potential common stock. The statement defines two earnings per share calculations, basic and diluted. The following table is a reconciliation of the numerator and denominator under each method:

FOR THE YEAR ENDED DECEMBER 31, 1998 (THOUSANDS EXCEPT PER SHARE DATA)	INCOME	SHARES	PER SHARE AMOUNT
Basic EPS:			
Net income applicable to common stock from continuing operations	$43,929	37,028	$1.19
Net income applicable to common stock	$43,929	37,028	$1.19
Assuming dilution:			
Net income applicable to common stock from continuing operations	$43,929	37,028	
Stock options	—	165	
Convertible preference stock	1,829	1,999	
Net income applicable to common stock	$45,758	39,192	$1.17

FOR THE YEAR ENDED DECEMBER 31, 1997 (THOUSANDS EXCEPT PER SHARE DATA)	INCOME	SHARES	PER SHARE AMOUNT
Basic EPS:			
Net income applicable to common stock from continuing operations	$29,331	35,492	$.83
Net income applicable to common stock	$29,331	35,492	$.83
Assuming dilution:			
Net income applicable to common stock from continuing operations	$29,331	35,492	
Stock options	—	156	
Convertible preference stock	2,076	2,190	
Net income applicable to common stock	$31,407	37,838	$.83

FOR THE YEAR ENDED DECEMBER 31, 1996 (THOUSANDS EXCEPT PER SHARE DATA)	INCOME	SHARES	PER SHARE AMOUNT
Basic EPS:			
Net income applicable to common stock from continuing operations	$38,407	33,707	$1.14
Loss from discontinued operations	(4,397)	33,707	(.13)
Net income applicable to common stock	$34,010	33,707	$1.01
Assuming dilution:			
Net income applicable to common stock from continuing operations	$38,407	33,707	
Stock options	—	21	
Convertible preference stock	2,342	2,490	
	$40,749	36,218	$1.12
Loss from discontinued operations	(4,397)	36,218	(.12)
Net income applicable to common stock	$36,352	36,218	$1.00

Sixteen I Segment Information

In June 1997, the FASB issued SFAS No. 131, "Disclosure about Segments of an Enterprise and Related Information," which requires that business segment financial information be reported in the financial statements utilizing the management approach. Those segments include utility investments, real estate and non-regulated business.

United Water's utility investments include United Water New Jersey, United Water New York, and the utility subsidiaries of United Waterworks and United Water Mid-Atlantic. These regulated utilities provide water and wastewater services to the public at large in areas where they possess franchises or other rights to provide such services. The utility subsidiaries are subject to rate regulation, generally by the regulatory authorities in the states in which they operate. In addition, the Company holds a 50% investment in the Northumbrian Partnership, which acquired a 20% interest in Northumbrian Water Group, a major investor-owned water and wastewater company in the United Kingdom.

United Properties Group is a non-regulated business engaged in real estate investment and development activities, including commercial office and retail properties, residential and commercial land development and sales, golf course operations and consulting services. United Properties Group owns a portfolio of real estate located in New Jersey, New York, Delaware, Idaho and Florida.

The Company's non-regulated sector consists primarily of a 50% investment in United Water Services, a 50/50 joint venture with Suez Lyonnaise des Eaux, which provides contract operations and maintenance services for water and wastewater facilities. In addition, United Water entered into public-private partnerships with the cities of Jersey City and Hoboken, New Jersey. Under these arrangements, the municipalities retain ownership of their systems while the Company operates and maintains them. Parent and elimination companies are also included in this segment.

(THOUSANDS OF DOLLARS)	UTILITY INVESTMENTS	REAL ESTATE	PARENT, NON-REGULATED WATER SERVICES AND ELIMINATIONS	CONSOLIDATED
1998				
Operating revenues	**$ 325,475**	**$16,196**	**$ 14,539**	**$ 356,210**
Depreciation and amortization	**35,594**	**1,593**	**2,763**	**39,950**
Interest expense	**39,361**	**1,742**	**4,814**	**45,917**
Equity earnings of affiliates	**17,103**	**—**	**(5,652)**	**11,451**
Provision for income taxes	**23,288**	**1,985**	**(5,823)**	**19,450**
Capital expenditures	**100,034**	**5,038**	**952**	**106,024**
Identifiable assets	**1,626,876**	**91,739**	**50,507**	**1,769,122**
1997				
Operating revenues	$ 313,346	$20,075	$ 17,988	$ 351,409
Depreciation and amortization	31,519	1,419	1,756	34,694
Interest expense	38,936	1,750	4,686	45,372
Equity earnings of affiliates	3,304	—	(2,991)	313
Provision for income taxes	21,546	2,439	(3,406)	20,579
Capital expenditures	83,342	2,431	1,004	86,777
Identifiable assets	1,512,966	88,388	56,988	1,658,342
1996				
Operating revenues	$ 299,283	$13,769	$ 18,993	$ 332,045
Depreciation and amortization	28,157	1,296	1,399	30,852
Interest expense	39,161	1,750	4,040	44,951
Equity earnings of affiliates	5,991	—	(1,374)	4,617
Provision for income taxes	26,924	1,066	(2,112)	25,878
Capital expenditures	75,726	2,831	2,914	81,471
Identifiable assets	1,461,302	90,212	30,583	1,582,097

Quarterly Financial Information (unaudited)

(THOUSANDS OF DOLLARS EXCEPT PER SHARE DATA)	QUARTER FIRST	SECOND	THIRD	FOURTH
1998				
Operating revenues	**$75,442**	**$86,219**	**$108,748**	**$85,801**
Operating income	**13,720**	**22,271**	**39,482**	**22,127**
Net income applicable to common stock	**3,134**	**11,042**	**19,500**	**10,253**
Net income per common share	**$ .09**	**$ .30**	**$ .52**	**$ .27**
Net income per common share – diluted	**$ .09**	**$ .30**	**$ .51**	**$ .27**
1997				
Operating revenues	$80,006	$87,761	$99,690	$83,952
Operating income	14,644	24,991	34,169	21,840
Net income applicable to common stock	4,102	11,244	6,464	7,521
Net income per common share	$ .12	$ .32	$ .18	$ .21
Net income per common share – diluted	$ .12	$ .31	$ .18	$ .21
1996				
Operating revenues	$69,759	$82,581	$97,871	$81,834
Operating income	14,092	24,415	33,920	23,272
Net income applicable to common stock	4,881	7,363	15,521	6,245
Net income per common share	$ .15	$ .22	$ .46	$ .18
Net income per common share – diluted	$ .15	$ .22	$ .44	$ .18

As disclosed in Note 2 to the consolidated financial statements, the Company recorded a net $10.3 million charge resulting from the "windfall profits" tax in the United Kingdom during the third quarter of 1997.
As disclosed in Note 3 to the consolidated financial statements, the Company settled the condemnation proceeding with the city of Rio Rancho. As a result, an after-tax gain of $4.3 million is included in the Company's 1996 first quarter earnings.

Report of Management

The consolidated financial statements included in this annual report have been prepared by and are the responsibility of management. The statements were prepared in conformity with generally accepted accounting principles considered appropriate in the circumstances and include amounts based on necessary judgments and estimates which management considers to be reasonable and appropriate. The financial statements of the company have been audited by its independent accountants, PricewaterhouseCoopers LLP. This audit, in the opinion of PricewaterhouseCoopers LLP, has been made in accordance with generally accepted auditing standards and their report on the fairness of the financial statements is included herein.

The company maintains a system of internal accounting controls designed to produce reliable financial statements and to provide reasonable assurance that the assets of the company are safeguarded from loss and unauthorized use. This system includes a program of internal audits to assure management that proper procedures and methods of operation are used to implement the plans, policies and directives of management.

The board of directors, through its audit committee, consisting of outside directors of the company, is responsible for reviewing the company's financial reporting and accounting practices. This committee meets periodically with management, internal auditors and the independent accountants to review their respective activities and the discharge of their responsibilities.

John J. Turner

John J. Turner
Treasurer
February 25, 1999

Report of Independent Accountants

To The Board of Directors and Shareholders of United Water Resources

In our opinion, the accompanying consolidated balance sheet and statement of consolidated capitalization and the related statements of consolidated income, common equity and cash flows present fairly, in all material respects, the financial position of United Water Resources and its subsidiaries at December 31, 1998 and 1997, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1998, in conformity with generally accepted accounting principles. These financial statements are the responsibility of United Water Resources' management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with generally accepted auditing standards which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
New York, New York
February 25, 1999

Record of Progress 1993-1998 (unaudited)

(THOUSANDS EXCEPT STATISTICAL AND PER SHARE DATA) AS OF AND FOR THE YEARS ENDED DECEMBER 31,	1998	1997	1996	1995	1994	1993
Selected Operating and Financial Data						
Operating revenues	$ 356,210	$ 351,409	$ 332,045	$ 319,536	$ 284,767	$191,703
Operating expenses	258,610	255,765	236,346	237,353	200,920	135,203
Operating income	97,600	95,644	95,699	82,183	83,847	56,500
Total interest and other expenses	30,163	41,389	26,801	41,984	31,419	22,488
Income from continuing operations before income taxes	67,437	54,255	68,898	40,199	52,428	34,012
Provision for income taxes	19,450	20,579	25,878	15,439	20,817	13,089
Income from continuing operations	47,987	33,676	43,020	24,760	31,611	20,923
Preferred and preference dividends	4,058	4,345	4,613	4,795	3,454	—
Net income applicable to common stock from continuing operations	$ 43,929	$ 29,331	$ 38,407	$ 19,965	$ 28,157	$ 20,923
Loss from discontinued operations	—	—	(4,397)	(2,622)	(270)	(945)
Net income applicable to common stock	$ 43,929	$ 29,331	$ 34,010	$ 17,343	$ 27,887	$ 19,978
Effective income tax rate	27.9%	36.4%	36.5%	36.8%	38.0%	36.0%
Utility plant	$1,540,564	$1,439,854	$1,349,194	$1,334,807	$1,272,446	$606,102
Accumulated depreciation	328,224	296,820	267,639	253,529	235,962	103,557
Net utility plant	1,212,340	1,143,034	1,081,555	1,081,278	1,036,484	502,545
Real estate and other properties	198,228	178,684	165,773	98,082	107,315	96,312
Total assets	$1,769,122	$1,658,342	$1,582,097	$1,516,708	$1,457,427	$740,526
Capitalization						
Common equity	$ 456,029	$ 418,601	$ 391,490	$ 358,302	$ 350,495	$202,110
Preferred and preference stock	89,282	95,579	102,261	107,091	107,173	32,840
Long-term debt	652,969	622,737	558,093	558,658	505,204	276,753
Total capitalization	$1,198,280	$1,136,917	$1,051,844	$1,024,051	$ 962,872	$511,703
Notes payable	$ 93,400	$ 74,925	$ 93,225	$ 43,500	$ 76,450	$ 15,500
Capitalization ratios						
Common equity	38.1%	36.8%	37.2%	35.0%	36.4%	39.5%
Preferred and preference stock	7.4%	8.4%	9.7%	10.4%	11.1%	6.4%
Long-term debt	54.5%	54.8%	53.1%	54.6%	52.5%	54.1%
Average cost of long-term debt	7.2%	7.4%	7.8%	7.5%	7.7%	7.7%
Coverages (SEC method)						
Utility coverages						
Earnings to fixed charges	2.94	2.70	2.85	2.48	2.62	2.50
Earnings to fixed charges and preferred stock dividends	2.42	2.15	2.28	1.96	2.09	2.23
United Water coverage						
Earnings to fixed charges	2.07	1.79	1.92	1.43	1.84	2.01
Utility plant additions*	$ 99,722	$ 83,321	$ 74,569	$ 70,227	$ 57,592	$ 15,986
Utility plant additions as percent of total capitalization*	8.3%	7.3%	7.1%	6.9%	6.0%	3.1%
Internally generated cash after dividends as percent of utility plant additions*	51.4%	51.4%	56.5%	39.3%	49.5%	130.1%
AFUDC as percent of utility net income	10.8%	9.1%	8.0%	5.5%	3.8%	3.4%

*Utility plant additions are net of AFUDC.

	1998	1997	1996	1995	1994	1993
Common Stock Data						
Net income per share	$ 1.19	$ .83	$ 1.01	$ .54	$ 1.01	$ 1.03
Net income per share—assuming dilution	$ 1.17	$ .83	$ 1.00	$ .54	$ 1.01	$ 1.03
Dividends paid per share	.93	.92	.92	.92	.92	.92
Dividend rate at year end	.96	.92	.92	.92	.92	.92
Equity per common share	12.05	11.53	11.33	10.90	11.20	10.00
Market value						
High	25.000	19.813	17.500	14.125	14.750	15.875
Low	15.750	15.000	12.000	11.750	12.250	14.000
Close	23.938	19.563	15.500	12.000	12.625	14.000
Market to book ratio	199%	170%	137%	110%	113%	140%
Dividend yield						
Market value (average)	4.6%	5.3%	6.2%	7.1%	6.8%	6.2%
Book value	7.7%	8.0%	8.1%	8.4%	8.2%	9.2%
Dividend payout ratio	78.2%	110.8%	91.1%	170.4%	91.1%	89.5%
Price/earnings ratio	20.1	23.6	15.3	22.2	12.5	13.6
Internally generated dividend coverage	2.5	2.3	2.4	1.9	2.2	2.2
Return on average common equity	10.2%	7.3%	9.3%	4.9%	9.4%	10.5%
Shareholders of record	18,035	18,399	18,651	18,980	19,602	18,729
Shares outstanding (thousands)						
Average	37,028	35,492	33,728	31,995	27,524	19,428
Year end	37,836	36,295	34,549	32,880	31,281	20,216
Selected Utility Data						
Water customers						
Residential	541,813	533,645	527,765	489,025	496,400	210,464
Commercial	54,846	53,327	52,783	52,132	51,981	23,962
Industrial	8,152	8,392	8,237	6,558	3,340	1,563
Total water customers	604,811	595,364	588,785	547,715	551,721	235,989
Wastewater customers	28,072	27,039	26,347	22,220	34,660	1,315
Utility revenues						
Residential	$205,754	$192,690	$179,077	$180,844	$160,318	$ 99,862
Commercial	86,994	80,992	80,672	76,769	66,761	38,395
Industrial	23,388	22,674	22,033	22,030	17,510	6,253
Public fire protection	13,284	12,839	12,360	11,859	10,733	8,007
Total utility revenues	$329,420	$309,195	$294,142	$291,502	$255,322	$152,517
Metered water sales (millions of gallons)						
Residential	54,380	49,797	49,212	52,439	49,141	27,818
Commercial	25,487	23,032	22,933	25,138	22,206	10,517
Industrial	11,309	10,534	10,703	11,899	7,597	1,957
Total metered water sales	91,176	83,363	82,848	89,476	78,944	40,292
Miles of water mains	7,522	7,339	7,314	7,174	7,472	2,981
Utility employees	1,154	1,140	1,119	1,140	1,282	567

Common Stock Data

(DOLLARS) QUARTER	STOCK PRICE HIGH	LOW	DIVIDEND
1998			
Fourth	**$25.000**	**$16.500**	**$.24**
Third	**19.250**	**16.375**	**.23**
Second	**18.438**	**15.750**	**.23**
First	**19.875**	**17.500**	**.23**
1997			
Fourth	$19.750	$16.000	$.23
Third	19.813	17.000	.23
Second	19.375	16.375	.23
First	18.500	15.000	.23
1996			
Fourth	$16.625	$14.625	$.23
Third	17.500	12.750	.23
Second	13.500	12.000	.23
First	13.250	12.000	.23

The high and low stock prices from January 1 to February 28, 1999, were $24.063 and $19.250.

Shareholder Information

CORPORATE HEADQUARTERS

United Water Resources
200 Old Hook Road
Harrington Park, NJ 07640-1799
Telephone 201 784 9434

WEB SITE

www.unitedwater.com

INVESTOR RELATIONS MANAGER

Cheryl L. DeMallie
Telephone 201 767 2811
Email: demallc@unitedwater.com

FORM 10-K

The annual report filed with the Securities and Exchange Commission is available to shareholders without charge upon request to Allan D. Shakley, Assistant Secretary, at the company's headquarters.

STOCK TRANSFER AND DIVIDEND DISBURSING AGENT AND REGISTRAR

Dividend Reinvestment and Stock Purchase Plan Correspondence:
ChaseMellon Shareholder Services, L.L.C.
PO Box 3336
South Hackensack, NJ 07606-1936
Attention: Investment Services

Optional Cash Payments ONLY:
ChaseMellon Shareholder Services, L.L.C.
Investor Services
PO Box 382009
Pittsburgh, PA 15250-8009

All Other Inquiries and Correspondence:
ChaseMellon Shareholder Services, L.L.C.
85 Challenger Road
Ridgefield Park, NJ 07660
Attention: Strategic Business Unit

Web Site: www.chasemellon.com
Telephone toll-free for all inquiries 800 230 2685
Telephone toll-free for individuals who are hearing and/or speech impaired 800 231 5469

1999 ANNUAL MEETING

United Water's 1999 annual meeting will be held on Monday, May 10 at 9:30 a.m., at the Park Ridge Marriott, in Park Ridge, NJ.

AGENT FOR ACCEPTANCE OF STOCK

ChaseMellon Shareholder Services, L.L.C.
120 Broadway
13th Floor
New York, NY 10271

INDEPENDENT ACCOUNTANTS

PricewaterhouseCoopers LLP
1177 Avenue of the Americas
New York, NY 10036

In keeping with our commitment to the environment, this report was printed on recycled paper.

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Directors

Donald L. Correll (E)
Chairman and Chief Executive Officer
United Water Resources

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Chairman, President and Chief Executive Officer
Sun Chemical Corporation

Frank J. Borelli (C,P)
Senior Vice President and
Chief Financial Officer
Marsh & McLennan Companies

Thierry Bourbie (C,E,P)
President
International Water Division
Lyonnaise des Eaux

Charles Chaumin (A)
Vice President
Americas
Lyonnaise des Eaux

Lawrence R. Codey (E)
President and Chief Operating Officer
Public Service Electric & Gas Co.

Peter Del Col (P)
Chairman
Colson Service Corporation

Robert L. Duncan, Jr., Esq. (A)
General Counsel
American Management
Association International

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Hampshire Management Company

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Chairman of the Board
Trigen Energy Corporation

Dennis M. Newnham (A,P)
President and Chief Executive Officer
The B. Manischewitz Company

Marcia L. Worthing (C,P)
Executive Vice President
Mullin & Associates

Committees
A) Audit
C) Compensation
E) Executive
P) Pension

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United Water Resources

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Chairman, President and
Chief Executive Officer

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Secretary

Richard B. McGlynn, Esq.
General Counsel

John J. Turner
Treasurer

Allan D. Shakley
Assistant Secretary

United Water Management and Services

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Chairman and Chief Executive Officer

Joseph Simunovich
President and Chief of Staff

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Vice President and General Counsel

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Secretary

United Water New Jersey

Frank J. De Micco
President

United Waterworks

Donald L. Correll
President

Robert J. Iacullo
Vice President

United Water Services

Donald L. Correll
Chairman

Jean Michel Brault
Vice Chairman and
Chief Executive Officer

David Sherman
President

United Properties Group

Michael C. J. Fallon
President

United Water®

200 Old Hook Road/ /Harrington Park/ /NJ 07640–1799/ /telephone 201 784 9434/ /www.unitedwater.com

[UNITED WATER RESOURCES INC. LETTERHEAD]

, 1999

Dear United Water Resources Inc. Stockholder:

The board of directors of UWR has entered into a merger agreement to merge our company with a subsidiary of Lyonnaise American Holding, Inc., thereby causing our company to become a wholly-owned subsidiary of LAH. LAH currently holds approximately 30.1% of the outstanding shares of UWR common stock and is a wholly-owned subsidiary of Suez Lyonnaise des Eaux.

We have scheduled a special meeting of the holders of the common stock and 5% series A cumulative convertible preference stock of United Water Resources, Inc. to approve the merger agreement. This special meeting will be held at [date, time and location of meeting].

At this important meeting, you will be asked to approve the acquisition by Lyonnaise American Holding, Inc. of the shares of UWR common stock (approximately 70%) which it does not already own through the merger of UWR into a wholly-owned subsidiary of LAH. If the merger is completed, you will receive

- $35.00 for each share of UWR common stock you own and
- $29.17 for each share of UWR series A preference stock you own immediately prior to the effective date of the merger.

In addition, under the merger agreement your board of directors has the right and intends to increase the regular quarterly dividend payable on UWR common stock above its customary dividend rate by an aggregate of $0.48 during the period between now and the completion of the merger. (Holders of UWR series A preference stock will not receive this increased dividend.) As a result of the merger and the increased special dividend during this period, you will receive as consideration for the merger a total of $35.48 for each share of UWR common stock that you own. The proposed consideration payable per share of UWR common stock, $35.00 (which does not take into account the $0.48 increase in dividends that shareholders will receive prior to the date that the merger becomes effective), represents a premium of 52.3% over the $22.98 per share average closing price of UWR common stock for the 30 trading days immediately preceding UWR's announcement on August 18, 1999 that it was engaged in merger negotiations. During this trading period, UWR common stock closed at a low of $21.37 per share and a high of $24.53 per share.

The board of directors of UWR unanimously approved the merger and has determined that the merger is advisable for, fair to, and in the best interests of, the UWR stockholders. **Your board of directors unanimously recommends that you vote "FOR" this transaction.**

We cannot complete the merger without the approval of each of (i) two-thirds of all of the outstanding shares of common stock of UWR not owned by Lyonnaise American Holding, Inc., (ii) two-thirds of all of the outstanding shares of UWR Series A Cumulative Convertible Preference Stock, and (iii) a majority of the shares of common stock voting at the special meeting. **As a result, your vote is very important.** Even if you plan to attend the special meeting, we urge you to mark, sign and date the enclosed proxy and return it promptly. You may also vote by telephone by calling the toll-free number on your proxy card. You have the option of revoking the proxy at any time or to vote your shares personally on request if you attend the meeting.

If you do not return the proxy card or vote by telephone and do not vote at the meeting, it will have the same effect as if you voted **AGAINST** the transaction. Your vote is important no matter how many shares you hold.

Yours very truly,

/s/ ______________________________
Donald L. Correll
Chairman and Chief Executive Officer

THIS TRANSACTION HAS NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION NOR HAS THE COMMISSION PASSED UPON THE FAIRNESS OR MERITS OF SUCH TRANSACTION NOR UPON THE ACCURACY OR ADEQUACY OF THE INFORMATION CONTAINED IN THIS DOCUMENT. ANY REPRESENTATION TO THE CONTRARY IS UNLAWFUL.

[UNITED WATER RESOURCES INC. LETTERHEAD]

NOTICE OF SPECIAL MEETING OF STOCKHOLDERS

TO BE HELD ON ,

To the holders of the common stock and Series A Cumulative
Convertible Preference Stock of UNITED WATER RESOURCES INC.:

NOTICE IS HEREBY GIVEN that a special meeting of the holders of the common stock and series A cumulative convertible preference stock of United Water Resources Inc., a New Jersey corporation (''UWR''), will be held at **[date, time and location of meeting]**, for the following purpose, which is more fully described in the accompanying proxy statement:

At the special meeting, you will be asked to consider and vote upon a proposal to adopt the Agreement and Plan of Merger, dated as of August 20, 1999 (the ''Merger Agreement''), by and among UWR, Lyonnaise American Holding, Inc. (''LAH''), LAH Acquisition Co., (''LAH Acquisition'') and Suez Lyonnaise des Eaux (''SLDE''). If the stockholders of UWR adopt the Merger Agreement and the merger is completed, LAH Acquisition Co. will be merged with and into UWR, with
(i) each outstanding share of UWR common stock being converted into the right to receive $35.00 in cash, without interest, and
(ii) each outstanding share of series A preference stock being automatically converted into the right to receive $29.17 in cash, without interest.

Adoption of the Merger Agreement requires the affirmative vote of each of (i) two-thirds of all of the outstanding shares of UWR common stock not owned by LAH or certain affiliates of LAH, (ii) two-thirds of all of the outstanding shares of UWR's series A cumulative convertible preference stock, and (iii) a majority of the shares of common stock voting at the special meeting.

Only holders of record of shares of common stock and series A preference stock at the close of business on , 1999 are entitled to notice of, and to vote at, the special meeting. A complete list of stockholders entitled to vote at the special meeting will be available for examination, for proper purposes, during ordinary business hours at UWR's corporate offices, 200 Old Hook Road, Harrington Park, New Jersey 07640, during the 10 days prior to the special meeting.

Under New Jersey law, stockholders of UWR do not have appraisal rights. Therefore, if you vote against the merger, but the merger is eventually approved, you will receive the $35.00 per share cash consideration payable in the merger rather than an appraised value of the shares you hold.

BY ORDER OF THE BOARD OF DIRECTORS

/s/ ______________________________
Douglas W. Hawes
Secretary

[Date of Proxy]

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This preliminary proxy statement includes the opinion of Morgan Stanley dated as of August 20, 1999. The definitive proxy statement will include an opinion of Morgan Stanley dated as of the date of the definitive proxy, which is anticipated to be substantially similar to the opinion dated August 20, 1999.

WHERE YOU CAN FIND MORE INFORMATION

UWR files annual, quarterly and special reports, proxy statements and other information with the Securities and Exchange Commission (the "SEC"). These reports, proxy statements and other information can be inspected and copied at the public reference facilities maintained by the SEC at Room 1024, Judiciary Plaza, 450 Fifth Street, N.W., Washington, D.C. 20549-1004 and at the following regional offices of the SEC: New York Regional Office, 7 World Trade Center, Suite 1300, New York, New York 10048 and Chicago Regional Office, 500 West Madison Street, Suite 1400, Chicago, Illinois 60661. Copies of this information can also be obtained by mail from the Public Reference Section of the Commission at Judiciary Plaza, 450 Fifth Street, N.W., Washington, D.C. 20549-1004 at prescribed rates or on the SEC's web site (http://www.sec.gov).

In addition, materials and information concerning UWR may also be inspected at the offices of The New York Stock Exchange, Inc., 20 Broad Street, 7th Floor, New York, New York 10005.

The SEC allows UWR to "incorporate by reference" information into this proxy statement, which means that UWR can disclose important information to you by referring you to another document filed separately with the SEC. The information incorporated by reference is deemed to be part of this proxy statement, except for any information superseded by information contained directly in this proxy statement. This proxy statement incorporates by reference the documents set forth below that were previously filed with the SEC by UWR (SEC File No. 1-8586):

- UWR's Annual Report on Form 10-K for the fiscal year ended December 31, 1998.
- UWR's Quality Report on Form 10Q for the quarterly period ended March 31, 1999.
- UWR's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 1999.
- UWR's Current Report on Form 8-K dated August 27, 1999.
- UWR's Current Report on Form 8-A dated August 27, 1999.
- the Prospectus Supplement dated August 31, 1999 filed pursuant to Rule 424 supplementing the Prospectus dated May 18, 1999 relating to UWR's Dividend Reinvestment and Stock Purchase Plan.

These documents contain important information about UWR and its financial condition. We also incorporate by reference any filing we will make with the SEC under Section 13(a), 13(c), 13(e), 14 or 15(d) of the Securities Exchange Act of 1934, as amended, between the date of this proxy statement and the date the special meeting is held. These other documents will be deemed to be incorporated by reference in this proxy statement and to be a part of it from the date they are filed with the SEC and will update and supersede any information previously disclosed.

You should rely only on the information contained in or incorporated by reference in this proxy statement in deciding how to vote on the Merger Agreement. No person is authorized to give any information or to make any representations in connection with the merger other than those contained in this proxy statement and you should not rely on any such information or representations given or made as having been authorized by UWR. The delivery of this proxy statement does not imply under any circumstances that the affairs of UWR or the information set forth herein are unchanged since the date of this proxy statement.

FORWARD-LOOKING STATEMENTS MAY PROVE INACCURATE

UWR has made forward-looking statements in this document (and in documents that are incorporated by reference) that are subject to risks and uncertainties. Forward-looking statements include the information concerning possible or assumed future results of operations of UWR. Also, when we use words such as ''believes,'' ''expects,'' ''anticipates'' or similar expressions, we are making forward-looking statements. Stockholders should note that many factors, some of which are discussed elsewhere in this document and in the documents that we incorporate by reference, could affect the future financial results of UWR and could cause those results to differ materially from those expressed in our forward-looking statements contained or incorporated by reference in this document. The factors that could cause actual results to differ materially from those indicated by such forward-looking statements include, but are not limited to, the following: preliminary information that may be subject to further and/or continuing review and adjustment; regulatory issues; changes in the economy; the impact of competition from other water services companies; the management of UWR's operations; variations in prices of materials used in the water services industry; growth opportunities for the companies' regulated and non-regulated businesses; conditions of the capital and equity markets; changes in the companies' accounting policies; abnormal weather conditions; inflation; exposure to environmental issues and liabilities; changes in environmental regulations; successful correction of any material Year 2000 problem or, alternatively, successful implementation of a contingency plan by the companies and any critical third party suppliers; and the other risks and uncertainties described from time to time in the companies' periodic reports filed with the SEC. UWR disclaims any obligation to update any forward-looking statement.

QUESTIONS AND ANSWERS ABOUT THE MERGER

Q: Why did the UWR board of directors decide to accept LAH's offer to acquire the rest of UWR's stock?

Your board of directors decided to accept LAH's offer because LAH offered a price for those shares which your board of directors believes represents significantly higher value for your shares than that which could be achieved at this time through other strategies.

Q: Why did the UWR board of directors decide that merging with LAH was the best method for maximizing stockholder value now?

The water industry in the United States is going through a period of rapid consolidation. Your board of directors determined that because of UWR's size and limited capital resources, it could not easily take advantage of growth opportunities through acquisitions of significant water utilities or services companies at the premiums that UWR would have to pay to grow through acquisitions and, as a result, might not remain competitive in the industry. In addition, your board determined that it may not be able to participate in public private partnerships that UWR may pursue in the future that require significant amounts of capital to be contributed by the private party. Your board determined that UWR stockholders could best benefit from the industry consolidation through a sale of UWR to, or a business combination of UWR with, a larger industry leader. In reviewing its alternatives, your board determined that LAH was willing to pay more for the remaining approximately 70% of the UWR shares it did not own than UWR was likely to receive in an auction or other sale of the company.

Q. What effect will the merger have on UWR's customers and employees?

Your board of directors believes that the merger will help position UWR to become one of the world's premier water services companies by providing strategic growth opportunities and access to cutting-edge technologies that will benefit the company and its customers and employees in a manner that UWR could not achieve on its own.

Q. What will I receive in the merger?

Holders of Common Stock

You will receive $35.00 in cash for each whole share of common stock held by you. In addition, under the merger agreement your board of directors has the right and intends to increase the quarterly dividend on UWR common stock above its customary dividend rate by up to $0.06 per share per quarter for each of the next three fiscal quarters beginning December 1, 1999, and pay a special dividend immediately prior to the merger in an amount equal to the difference between $0.48 and the aggregate amount of the additional quarterly dividends. When combined, the increased regular quarterly dividends and special dividend will result in an aggregate dividend increase of $0.48 per share that is held throughout this period. Therefore, the total cash consideration you will receive for each share of common stock, including the increased dividend, is $35.48 (fractional shares of common stock will be paid a proportional amount). The proposed consideration payable per share of UWR common stock, $35.00 (which does not take into account the $0.48 increase in dividends that stockholders will receive prior to the date that the merger becomes effective), represents a premium of 52.3% over the $22.98 per share average closing price of UWR common stock for the 30 trading days immediately preceding UWR's announcement on August 18, 1999 that it was engaged in merger negotiations. During this trading period, UWR common stock closed at a low of $21.37 per share and a high of $24.53 per share.

Holders of Series A Preference Stock

For each share of series A preference stock held by you, you will receive an amount in cash equal to $29.17. (This amount is equal to $35.00 multiplied by the .83333 shares of common stock into which each share of series A preference stock is convertible.) Holders of series A preference stock will not receive any additional dividend in connection with the merger.

Q: Does the merger have to be approved by the UWR stockholders?

Yes, the merger must be approved by each of (i) two-thirds of all of the outstanding common shares of UWR not owned by LAH, (ii) two-thirds of all of the outstanding shares of UWR series A preference stock, and (iii) a majority of the shares of common stock voting at the special meeting. These approvals will be sought at the special stockholders meeting to be held [date, time and location of special meeting].

Q: Will I still be a stockholder of UWR following the merger?

No. In the merger, you will receive cash in exchange for your UWR shares. Following the merger, UWR will be a wholly-owned subsidiary of LAH and its shares will be delisted from the New York Stock Exchange.

Q. What do I need to do now?

Just mark, sign, date and mail your proxy card in the enclosed return envelope as soon as possible. That way, your shares can be represented at the UWR special meeting. You may also vote by telephone by calling the toll-free number on your proxy card. If your shares are held in your broker's street name, then follow the instructions they will provide. If you intend to vote by telephone, do not return the proxy card.

The merger cannot be completed unless (i) two-thirds of all of the outstanding common shares of UWR not owned by LAH, (ii) two-thirds of all of the outstanding shares of UWR series A preference stock, and (iii) a majority of the shares of common stock voting at the special meeting approve the Merger Agreement. Failure to vote your shares will have the same effect as a vote "AGAINST" the merger. **Your vote is very important.**

The board of directors of UWR recommends voting "FOR" approval of the Merger Agreement.

Q: Should I send in my stock certificates now?

No. **Do not send in your stock certificates now.** If the merger is completed, you will receive written instructions on how to exchange them.

Q. Will my broker vote my shares if my shares are held in my broker's street name?

No. Your broker will not be able to vote your shares without instructions from you. Therefore, you need to tell your broker how to vote your shares by following the instructions provided by your broker.

If you do not instruct your broker on how to vote, it will have the same effect as a vote "AGAINST" the merger.

Q. Can I change my vote after I have mailed in my signed and dated proxy card or voted by telephone?

Yes. You may revoke your proxy at any time before your shares are voted (i) by attending the special meeting and voting in person or (ii) by delivering a duly executed proxy, dated later than the proxy previously delivered, to the Secretary of UWR, 200 Old Hook Road, Harrington Park, New Jersey, 07640 or (iii) by telephone if you have previously voted by telephone. Unless revoked in a manner set forth above, proxies in the form enclosed will be voted at the special meeting in accordance with your instructions.

Q. What are the federal income tax consequences of the merger?

You will be taxed on your receipt of the cash given to you for your shares to the extent that the amount you receive exceeds your tax basis in your UWR stock. Please read the more detailed description of the federal income tax consequences of the merger on pages 32—33.

Q. Do I have appraisal rights for my shares if the merger is completed?

No. An appraisal right permits stockholders to receive payment for their shares in an amount determined by an independent appraisal rather than the consideration which they otherwise would receive in the transaction. Under New Jersey state law, UWR stockholders do not have appraisal rights in the merger. Therefore, if you vote against the merger but the merger is nonetheless approved by the requisite votes of the stockholders, you will still receive the

$35.00 per share cash consideration payable for common stock or $29.17 payable for series A preference stock rather than an appraised value of the shares you hold.

Q. What regulatory approvals are needed for the merger?

The merger must be approved by the public utility commissions (or similar regulators) in a number of the states in which UWR operates. Clearance under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 is also necessary.

Q. What other matters will be voted on at the special meeting?

We do not expect any matters other than the approval of the merger to be presented to stockholders for vote at the special meeting.

Q. When is the merger expected to be completed?

We are working to complete all aspects of the merger as quickly as possible. We currently expect to complete the merger during the first half of the year 2000.

Q. When will I receive my cash proceeds if the merger is approved and completed?

After the effective time of the merger, instructions and forms will be forwarded to you explaining how and when to tender your shares. The exchange agent will remit your cash proceeds upon verification of this documentation and receipt of your share certificates. No action is required on your part to tender shares held in the UWR common stock plans such as the Dividend Reinvestment and Stock Purchase Plans. Shares held in these plans are in book entry form. The exchange agent will distribute to you the cash proceeds for the book entry form shares based on your account balance at the effective time of the merger without any further action by you.

Q. Whom should I call if I have any additional questions?

UWR stockholders may call Investor Relations at (800) 422-9817.

SUMMARY

The following is a summary of selected information contained elsewhere in this proxy statement and may not contain all of the information that is important to you. To understand the merger fully and for a more complete description of the terms of the merger, you should read carefully this entire proxy statement and the other documents to which we have referred you. See "Where You Can Find More Information" on p.1 of this proxy statement. For a review of the actual terms of the merger, the Merger Agreement is attached to this proxy statement as Annex A. In this document, the term UWR refers to either UWR before the completion of the merger or UWR as the surviving corporation in the merger, whichever the context requires. In addition, the term "stockholder" of UWR refers to holders of UWR common stock and/or UWR series A preference stock, whichever the context requires. We have included page references parenthetically referring you to more complete descriptions of the topics presented in the summary.

The Companies (Pages 43-47)

United Water Resources Inc. (UWR)
200 Old Hook Road
Harrington Park, New Jersey 07640
(201) 784-9434

UWR is a holding company primarily engaged in water-related businesses. As the second largest investor-owned water services company in the United States, UWR provides water and wastewater services through its regulated utilities and nonregulated contract operations (some of which are owned jointly with LAH) to over 7.5 million people in more than 400 communities in 19 states. UWR also has investments in joint venture companies providing water services in Canada and Mexico, in which LAH is a majority owner, and has an investment in a water services company in the United Kingdom made in partnership with SLDE. In addition, the company owns and manages real estate investments through a wholly-owned subsidiary. UWR has been listed on the New York Stock Exchange since 1889 and has paid cash dividends on its common stock continuously since 1886.

Suez Lyonnaise des Eaux (SLDE)
1, rue d'Astorg
75008 Paris
France

SLDE, a *societe anonyme* organized and existing under the laws of the Republic of France, operates private infrastructure services in more than 120 countries, providing electricity and natural gas, waste services, communications services, and water services and maintains interests in construction and capital investments. SLDE was formed from the 1997 merger of Compagnie de Suez (builder of the Suez Canal) and Lyonnaise des Eaux. SLDE's registered office is located at 72 Avenue de la Liberte, 92022 Nanterre Cedex, France, and the principal address of SLDE's water division is 18 Square Edouard VII, 75316 Paris Cedex 09, France.

Lyonnaise American Holding, Inc. (LAH)
2000 First State Boulevard
Wilmington, Delaware 19804-0507
(201)767-2851

LAH is a Delaware corporation with its principal business as a holding company of (i) its ownership interest in UWR, (ii) 50% of the voting interest in United Water Services LLC, a Delaware limited liability company which provides services in the water and wastewater industries to municipalities in the United States, (iii) majority interests in United Water Services Canada L.P., an Ontario, Canada limited partnership, and United Water Services Mexico LLC, a Delaware limited liability company, which provide services in the water and wastewater industries to municipalities in Canada and Mexico, respectively, and (iv) a 49% interest in Technologia y Servicios De Agua, S.A., a Mexican company which provides certain water services to the city of Mexico City, Mexico. All of the issued and outstanding shares of capital stock of LAH are owned beneficially and of record by SLDE. The principal business mailing address of LAH is c/o United Water Services LLC, 200 Old Hook Road, Harrington Park, New Jersey 07640, and the address of its principal office is 2000 First State Boulevard, Wilmington, Delaware 19804-0508.

LAH Acquisition Co. (LAH Acquisition)
c/o United Water Services LLC
200 Old Hook Road
Harrington Park, New Jersey 07640

LAH Acquisition is a wholly-owned special purpose subsidiary of LAH, formed under the laws of the State of New Jersey solely for the purpose of the merger. LAH Acquisition has not conducted any business other than in connection with the Merger Agreement. All of the issued and outstanding shares of capital stock of LAH Acquisition are owned beneficially and of record by LAH. The principal business mailing address of LAH Acquisition Co. is c/o United Water Services LLC, 200 Old Hook Road, Harrington Park, New Jersey 07640, and the address of its principal office is 1013 Centre Road, Wilmington, Delaware 19805-1297.

The UWR Special Meeting (Pages 13-14)

Date, Time and Place. The special meeting of the holders of UWR common stock and the UWR series A preference stock will be held together at **[time, date and location of meeting].**

Purpose of the Special Meetings. The purpose of the special meetings is to consider and vote on adoption of the Merger Agreement, pursuant to which, among other things, UWR will become a wholly-owned subsidiary of LAH and the stockholders of UWR will receive the cash consideration described in this summary on page 34.

Voting Rights. The board of directors of UWR has fixed the close of business on , as the record date for the determination of UWR stockholders entitled to notice of, and to vote at, the special meeting. As of the record date, UWR had [38,867,960] shares of common stock outstanding and [1,955,984] shares of series A preference stock outstanding. Holders of shares of common stock and series A preference stock are entitled to one vote for each share of stock held of record at the close of business on , . *See "THE SPECIAL MEETING—Voting Rights."*

Vote Required. The adoption of the Merger Agreement will require the approval of each of (i) two-thirds of all of the outstanding shares of common stock not owned by LAH or its affiliates, (ii) two-thirds of all of the outstanding shares of series A preference stock, and (iii) a majority of the shares of common stock voting at the special meeting. *See "THE SPECIAL MEETING—Vote Required" and "THE MERGER—Interests of Certain Persons in the Merger."*

The UWR board of directors Unanimously Recommends that UWR Stockholders Vote "For" Approval of the Merger Agreement.

Stock Ownership of Management. On the record date, the directors and executive officers of UWR and their affiliates beneficially owned [245,555] shares of common stock (excluding unexercised options), or approximately 0.9% of the voting power of the common stock outstanding on the record date. It is expected that all current directors and executive officers of UWR will vote the shares of common stock beneficially owned by them FOR the merger.

Stock Ownership of LAH. On the record date, LAH and its affiliates beneficially owned [11,687,024] shares of common stock, or approximately 30.1% of the voting power of the common stock outstanding on the record date, and [1,919,210] shares of series A preference stock, or approximately 98.1% of the voting power of the series A preference stock outstanding on the record date. It is expected that LAH and its affiliates will vote the shares of common stock and series A preference stock owned by them FOR the merger. However, because in addition to the approval of a majority of the shares of common stock voting at the special meeting, the merger must be approved by two-thirds of the outstanding shares of common stock not owned by LAH or its affiliates, the vote by LAH of its common stock of UWR will not be sufficient to determine the outcome at the special meeting of common stockholders. Because LAH and its affiliates own more than two-thirds of the outstanding series A preference stock, the vote by LAH and its affiliates of their series A preference shares in favor of the merger will be sufficient to provide the requisite vote at the special meeting of LAH's series A preference stock.

Voting of Proxies. All shares of common stock and series A preference stock represented by a properly executed proxy received in time for the special meeting will be voted in the manner specified in the proxy. Proxies that do not contain any instruction to vote for or against or to abstain from voting on a particular matter will be voted in accordance with the recommendation of the board of directors. *See "THE SPECIAL MEETING—Voting and Revocation of Proxies."*

It is not expected that any matter other than that referred to herein will be brought before the stockholders at the special meeting. If, however, other matters are properly presented, the persons named as proxies will use their best judgment in voting on these matters.

Adjournments; Revocability of Proxies. If the special meeting is adjourned, approval of the Merger Agreement will be considered and voted upon by stockholders at the reconvened meeting, if any.

You may revoke your proxy at any time before your shares are voted (i) by attending the special meeting and voting in person or (ii) by delivering a signed proxy relating to the merger, dated later than the proxy previously delivered, to the Secretary of UWR, 200 Old Hook Road, Harrington Park, New Jersey 07640 or (iii) by telephone if you have previously voted by telephone.

Solicitation of Proxies. The cost of soliciting proxies will be paid by UWR. Arrangements will be made to furnish copies of proxy materials to fiduciaries, custodians and brokerage houses for forwarding to beneficial owners of common stock. UWR has retained Georgeson and Company Inc. to assist in the solicitation of proxies. *See "THE SPECIAL MEETING—Solicitation of Proxies."*

Do *not* send your stock certificates with your proxy cards.

The Merger (Pages 15-34)

Overview. At the effective time of the merger, LAH Acquisition will be merged with and into UWR and UWR will continue as the surviving corporation. In the merger, all shares of UWR common stock and all shares of UWR series A preference stock owned by UWR, LAH or any of their respective wholly-owned subsidiaries will be canceled without consideration. All shares of UWR common stock and UWR series A preference stock not owned by UWR, LAH or any of their wholly-owned subsidiaries will be converted to the right to receive cash as follows:

- Each share of UWR common stock will be converted into the right to receive $35.00
- Each share of UWR series A preference stock will be converted into the right to receive $29.17.

As a result of the merger, UWR will become a wholly-owned subsidiary of LAH.

Background of, and Reasons for, the Merger.

You should review the factors considered by UWR's board of directors when deciding whether to approve the merger set out on pages 15 through 34.

Recommendation of the UWR Board of Directors. Your board of directors, with its LAH-affiliated members first abstaining and then joining in the vote, has unanimously approved the merger and recommends that the stockholders of UWR vote "FOR" the adoption of the Merger Agreement. For a discussion of the factors considered by your board in reaching its decision, *see "THE MERGER—Background of the Merger" and "THE MERGER—Reasons for the Merger."*

Opinion of UWR's Financial Advisor. Morgan Stanley & Co. Incorporated, UWR's financial advisor, has delivered written opinions to your board that as of August 20, 1999 and again on the date of this proxy statement, the merger consideration is fair, from a financial point of view, to the holders of UWR common stock, other than LAH. These opinions are not intended to be recommendations to any UWR stockholder as to how to vote. We have attached a copy of Morgan Stanley's opinion dated the date of this proxy statement as Annex B to this proxy statement. You should read this opinion carefully in its entirety. *See "THE MERGER—Opinions of UWR's Financial Advisor."*

Interests of Certain Persons in the Merger. In considering the recommendation of your board of directors with respect to the merger, you should be aware that certain directors and executive officers of UWR have interests that may conflict with the interests of other stockholders in the merger. Your board was aware of these potential conflicts and considered them along with other matters in recommending that you vote to approve the merger.

Federal Income Tax Consequences. A portion of the amounts received by UWR stockholders in exchange for their shares of UWR common stock and series A preference stock will be taxable for U.S. federal income tax purposes and may also be taxable under applicable state, local, foreign and other tax laws. **Stockholders are urged to consult their own tax advisers to determine the particular tax consequences to them (including the application and effect of any state, local or foreign income or other tax laws) resulting from the merger.**

Regulatory Matters. In order to complete the merger, we must receive certain federal clearances and state regulatory approvals. While there is no guarantee as to when, or whether, these regulatory approvals will be obtained, it is expected that the necessary approvals will be obtained during the first half of the year 2000.

Absence of Appraisal Rights. Stockholders of UWR do not have the right under New Jersey law to obtain an appraised value for their shares in place of the $35.00 per share cash payment for common stock or $29.17 payable for series A preference stock provided in the Merger Agreement.

The Merger Agreement (Pages 34-43)

Effective Time and Effects of the Merger. The merger will take place as soon as practicable, but in any event not later than the second business day after the satisfaction or waiver of the conditions set forth in the Merger Agreement, unless another date is agreed to by UWR and LAH. *See "THE MERGER AGREEMENT—Effective Time of the Merger" and "Effects of the Merger."*

Merger Consideration. At the effective time of the merger, each issued and outstanding share of UWR common stock (other than shares owned by UWR as treasury stock or shares owned, directly or indirectly, by UWR, LAH or any of their respective wholly-owned subsidiaries) shall be converted into the right to receive $35.00, without interest.

As of the effective time of the merger, each issued and outstanding share of series A preference stock (other than shares owned, directly or indirectly, by UWR, LAH or any of their respective wholly-owned subsidiaries) will be converted into the right to receive \$29.17 in cash, without interest. (This amount is equal to \$35.00 multiplied by the .83333 shares of common stock into which each share of series A preference stock is convertible.)

Increased Dividends. Under the Merger Agreement, the UWR board has the right and intends to increase the regular quarterly dividends payable on UWR common stock for each of the three fiscal quarters beginning December 1, 1999 by up to \$0.06 per share. This would increase the regular quarterly dividend from \$0.24 per quarter to up to \$0.30 per quarter. In addition, and assuming that the merger will be completed, the UWR board intends to pay a special dividend immediately prior to the effective time of the merger equal to the difference between \$0.48 and the aggregate amount of additional quarterly dividends paid.

Representations and Warranties. The Merger Agreement contains representations and warranties by UWR and LAH that are customary for a merger of this kind. *See "THE MERGER AGREEMENT—Representations and Warranties."*

Conduct of Business Prior to the Effective Time. UWR has agreed that until the merger is completed, it will carry on its businesses (including the businesses of its subsidiaries) in substantially the same manner as previously conducted. UWR has also agreed that, among other things, it will terminate the issuance or distribution of shares under the UWR Dividend Reinvestment and Stock Purchase Plan at the earliest possible date, limit its acquisitions of other businesses, limit the sale of certain assets, continue current accounting and tax practices and refrain from taking certain specified actions out of the ordinary course of business without the consent of LAH. *See "THE MERGER AGREEMENT—Certain Pre-Closing Covenants."*

Conditions to Closing. The obligations of UWR, LAH and LAH Acquisition to consummate the merger are subject to a number of conditions, including obtaining the required UWR stockholder approvals, obtaining the required regulatory approvals and the absence of any injunction or other legal restraint or prohibition preventing the consummation of the merger. *See "THE MERGER AGREEMENT—Conditions to the Consummation of the Merger."*

Termination. The Merger Agreement may be terminated by UWR or LAH prior to the merger becoming effective under certain circumstances, some of which would require UWR to pay LAH a termination fee of \$42 million. *See "THE MERGER AGREEMENT—Termination"* and *"THE MERGER AGREEMENT—Termination Fees and Expenses."*

Amendment. The Merger Agreement may be amended in writing by the parties at any time before or after the UWR stockholders approve the merger and prior to the effective time of the merger. However, after stockholder approval, no amendment may be made which would alter or change the rights of UWR stockholders, except for alterations or changes that could otherwise be adopted by the board of directors without the further approval of UWR stockholders.

Selected Historical Financial Information

The following table sets forth selected consolidated historical financial data of UWR and has been derived from and should be read in conjunction with the audited consolidated financial statements of UWR for each of the five years ended December 31, 1998 and the unaudited interim consolidated financial statements of UWR for the nine months ended September 30, 1999 and 1998, including the respective notes thereto. In the opinion of management, all adjustments, consisting of normal recurring accruals considered necessary for a fair presentation have been included in the unaudited interim data. Interim results for the nine months ended September 30, 1999 are not necessarily indicative of results which may be expected for future periods, including the year ended December 31, 1999.

	Nine months ended September 30,		Year ended December 31,				
	1999	1998	1998	1997	1996	1995	1994
			(In thousands, except per share data)				
Consolidated Income Statement Data:							
Operating revenues from continuing operations		$ 270,409	$ 356,210	$ 351,409	$ 332,045	$ 319,536	$ 284,767
Operating income		75,473	97,600	95,644	95,699	82,183	83,847
Income from continuing operations		36,764	47,987	33,676	43,020	24,760	31,611
Preferred and preference stock dividends		3,088	4,058	4,345	4,613	4,795	3,454
Net income from continuing operations	—	33,676	43,929	29,331	38,407	19,965	28,157
Loss from discontinued operations	—	—	—	—	(4,397)	(2,622)	(270)
Net income	$—	$ 33,676	$ 43,929	$ 29,331	$ 34,010	$ 17,343	$ 27,887
Basic earnings/(loss) per share							
From continuing operations		$ 0.91	$ 1.19	$ 0.83	$ 1.14	$ 0.62	$ 1.02
From discontinued operations	—	—	—	—	(0.05)	(0.08)	(0.01)
From disposal of discontinued operations	—	—	—	—	(0.08)	—	—
Basic earnings/(loss) per share	$—	$ 0.91	$ 1.19	$ 0.83	$ 1.01	$ 0.54	$ 1.01
Weighted average common shares outstanding		36,848	37,028	35,492	33,707	31,995	27,524
Diluted earnings/(loss) per share							
From continuing operations		$ 0.90	$ 1.17	$ 0.83	$ 1.12	$ 0.62	$ 1.02
From discontinued operations	—	—	—	—	(0.04)	(0.08)	(0.01)
From disposal of discontinued operations	—	—	—	—	(0.08)	—	—
Diluted earnings/(loss) per share	$—	$ 0.90	$ 1.17	$ 0.83	$ 1.00	$ 0.54	$ 1.01
Weighted average common shares outstanding		39,023	39,192	37,838	36,218	31,995	27,524
Dividends declared per common share		0.69	0.93	0.92	0.92	0.92	0.92
Balance Sheet Data: (at end of period)							
Total assets		1,719,857	1,769,122	1,658,342	1,582,097	1,516,708	1,457,427
Long-term obligations		618,714	652,969	622,737	558,093	558,658	505,204
Stockholders' equity		537,072	545,311	514,180	493,751	465,393	457,668
Book value per common share		11.95	12.05	11.53	11.33	10.90	11.20

Price of UWR Common Stock and Dividends

UWR's common stock is traded on the New York Stock Exchange under the symbol "UWR." The high and low sales prices per quarter for UWR's common stock through the third quarter of 1999, and for the years of 1998, 1997 and 1996 and the dividends paid on the common stock in each quarter, were as follows:

QUARTER	STOCK PRICE HIGH	STOCK PRICE LOW	DIVIDEND
1999			
Fourth through [October 4, 1999]	$33.000	$32.625	$
Third	32.938	20.750	.24
Second	23.688	20.000	.24
First	24.062	18.438	.24
1998			
Fourth	$25.000	$16.500	$.24
Third	19.250	16.375	.23
Second	18.438	15.750	.23
First	19.875	17.500	.23
1997			
Fourth	$19.750	$16.000	$.23
Third	19.813	17.000	.23
Second	19.375	16.375	.23
First	18.500	15.000	.23
1996			
Fourth	$16.625	$14.625	$.23
Third	17.500	12.750	.23
Second	13.500	12.000	.23
First	13.240	12.000	.23

On August 17, 1999, the last trading day before public announcement that UWR was engaged in merger negotiations, the last sale price of UWR common stock on the New York Stock Exchange Composite Transactions Tape was $24.53 per share.

On [October 4,] 1999, the most recent practicable date prior to the printing of this proxy statement, the last sale price of common stock as reported on the New York Stock Exchange Composite Transactions Tape was $33.000 per share.

THE SPECIAL MEETING

Date, Time and Place

The special meetings of the holders of UWR common stock and series A preference stock to vote on adoption of the Merger Agreement will be held together at **[time, place and location of the special meeting]**.

Purpose of the Special Meeting

The purpose of the special meeting of UWR common stockholders and holders of series A preference stock is to consider and vote upon a proposal to adopt the Merger Agreement entered into among UWR, LAH, SLDE and LAH Acquisition, a wholly-owned subsidiary of LAH.

Record Date; Voting Rights

The board of directors of UWR has fixed the close of business on   ,   as the record date to determine who receives notice of and who may vote at the special meeting. Only holders of record of shares of common stock and series A preference stock at the close of business on the record date will be entitled to notice of, and to vote at, the special meeting or any adjournment or postponement thereof.

As of the record date, UWR had [38,867,960] shares of common stock outstanding, which were held by [17,402] holders of record, and [1,955,984] shares of series A preference stock outstanding, which were held by [27] holders of record. Holders of shares of common stock are entitled to one vote for each share of common stock held of record at the close of business on the record date. Holders of shares of series A preference stock are entitled to one vote for each share of series A preference stock held of record at the close of business on the record date. The presence, in person or by valid proxy, of the holders of a majority of all shares entitled to vote at the special meeting of the common stockholders of UWR is necessary to constitute a quorum at the special meeting of the common stockholders. The presence, in person or by valid proxy, of the holders of a majority of all shares entitled to vote at the special meeting of the series A preference stockholders of UWR is necessary to constitute a quorum at the special meeting of the series A preference stockholders. For purposes of determining the presence of a quorum, abstentions and shares represented by a proxy from a broker or nominee indicating that no instructions have been received from the beneficial owner or other person entitled to vote the shares (''broker non-votes'') will be counted as shares present for quorum purposes. However, neither abstentions nor broker non-votes will be counted as votes cast for purposes of determining whether the Merger Agreement has received sufficient votes for approval and, therefore, will have the effect of a vote against the proposal that stockholders adopt the Merger Agreement.

If UWR does not receive by the time scheduled for the special meeting a sufficient number of signed proxies to enable adoption of the Merger Agreement, it may propose one or more adjournments or postponements of the special meeting to permit continued solicitation of proxies. Adjournment or postponement of the special meeting will be proposed only if the UWR board of directors believes that additional time to solicit proxies may permit the receipt of sufficient votes to adopt the Merger Agreement. It is anticipated that any such adjournment or postponement will be for a short period of time, but in no event for more than 30 days. Any stockholder may revoke his or her proxy during any period of adjournment or postponement in the manner described below.

Vote Required

The affirmative vote of the holders of each of (i) two-thirds of all of the outstanding shares of UWR common stock not owned by LAH or certain affiliates of LAH, (ii) two-thirds of all of the outstanding shares of series A preference stock, and (iii) a majority of the shares of common stock voting at the special meeting is required to adopt the Merger Agreement. As of September 30, 1999, directors and executive officers of UWR and their affiliates, as a group, beneficially held 245,555 shares of common stock (excluding unexercised options), representing less than 0.9% of the outstanding shares of common stock entitled to vote at the UWR special meeting. The directors and executive officers of UWR have indicated that they intend to vote such shares of common stock in favor of the proposal that the stockholders of UWR adopt the Merger Agreement.

On the record date, LAH and its affiliates beneficially owned [11,687,024] shares of common stock, or approximately 30.1% of the voting power of the common stock outstanding on the record date, and [1,919,210] shares of series A preference stock, or approximately 98.1% of the voting power of the series A preference stock outstanding on the record date. It is expected that LAH and its affiliates will vote the shares of common stock and series A preference stock owned by them FOR the merger. However, because, in addition to the approval of a majority of the shares of common stock voting at the special meeting, the merger must be approved by two-thirds of the outstanding shares of common stock not owned by LAH or its affiliates, the vote by LAH of its common stock of UWR will not be sufficient to determine the outcome at the special meeting of common stockholders. Because LAH owns more than two-thirds of the outstanding series A preference stock, a vote by LAH in favor of the merger, will be sufficient to provide the requisite vote at the special meeting of LAH's series A preference stock. LAH's sole stockholder has already approved the Merger Agreement.

Voting and Revocation of Proxies

Proxies in the form accompanying this proxy statement are solicited by UWR's board of directors. Shares of common stock and series A preference stock represented by valid proxies, which have not been revoked, will be voted at the special meeting in accordance with the instructions indicated on the proxies. If no instructions are indicated, such proxies will be voted "FOR" adoption of the Merger Agreement.

The UWR board of directors is not aware of any matters other than those specifically stated in this proxy statement that are to be presented for action at the special meeting. If any other matters are properly presented at the special meeting for action, including the adjournment of the special meeting, the persons named in the proxies will have discretion to vote on those matters in accordance with their best judgment. Any adjournment of the special meeting of the holders of UWR common stock will require the affirmative vote of the holders of a majority of the shares of common stock represented at the special meeting and any adjournment of the special meeting of the holders of UWR series A preference stock will require the affirmative vote of the holders of a majority of the shares of series A preference stock represented at the special meeting (regardless of whether those shares of common stock or series A preference stock constitute a quorum).

If you execute a proxy you have the power to revoke it at any time before it is voted. You may revoke your proxy (i) by attending the special meeting and voting in person or (ii) by delivering a new proxy dated later than your earlier proxy, to the Secretary of UWR, 200 Old Hook Road, Harrington Park, New Jersey 07640 or (iii) by telephone if you previously voted by telephone.

Cost of Solicitation of Proxies

UWR will bear the cost of the solicitation of proxies and the cost of printing and mailing this proxy statement. Arrangements will also be made with brokerage houses and other custodians, nominees and fiduciaries to forward solicitation material to the beneficial owners of shares held of record by such persons at UWR's expense. In addition, UWR has retained Georgeson and Company Inc. to assist in the solicitation of proxies for a fee of $8,000 and reimbursement for out-of-pocket expenses.

Holders of UWR stock should *not* send their stock certificates with their proxy cards. If the merger is consummated, we will inform you of the procedures for the exchange of your UWR stock certificates for the cash consideration to which you will be entitled. ***See "THE MERGER AGREEMENT—Exchange of Certificates."***

THE MERGER

This section of the proxy statement, as well as the next section entitled "The Merger Agreement," describes certain aspects of the merger. These sections highlight key information about the merger and the Merger Agreement but they may not include all the information that you would like to know. The Merger Agreement is attached as Annex A to this proxy statement. We urge you to read the Merger Agreement in its entirety.

Overview

On August 20, 1999, UWR, LAH, LAH Acquisition and SLDE entered into an Agreement and Plan of Merger. This agreement is referred to in this proxy statement as the "Merger Agreement." The Merger Agreement contemplates a merger in which LAH Acquisition, a wholly-owned subsidiary of LAH, will merge into UWR, with UWR as the surviving corporation. After the merger, UWR would continue to conduct its businesses as a wholly-owned subsidiary of LAH.

The merger is subject to the approval of UWR stockholders. The affirmative vote of each of two-thirds of all of the outstanding shares of UWR common stock (other than shares owned by LAH or certain affiliates of LAH), (ii) and two-thirds of all of the outstanding shares of series A preference stock, and (iii) a majority of the shares of common stock voting at the special meeting is required in order to consummate the merger. In addition, completion of the merger is subject to obtaining approval under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, and approval from a number of state utility commissions.

In this proxy statement, we refer to the time when the merger is completed as the "effective time" of the merger.

At the effective time of the merger, each issued and outstanding share of UWR common stock (other than shares owned, directly or indirectly, by UWR, LAH or any of their respective wholly-owned subsidiaries) will be converted into the right to receive $35.00, without interest.

At the effective time of the merger, each issued and outstanding share of series A preference stock (other than shares owned, directly or indirectly, by UWR, LAH or any of their respective wholly-owned subsidiaries) will be converted into the right to receive $29.17 in cash, without interest. (This amount is equal to $35.00 multiplied by the .83333 shares of common stock into which each share of series A preference stock is convertible.)

Certain Effects of the Merger

If the merger is consummated, the interest of LAH in UWR's net book value and net earnings will equal 100% and LAH will be entitled to all benefits resulting from such interest, including all income generated by UWR's operations and any future increase in UWR's value. Similarly, LAH will also bear the risk of losses generated by UWR's operations and any future decrease in the value of UWR after the merger. From the effective time of the merger, current stockholders of UWR will cease to have any equity interest in UWR, will not have the opportunity to participate in the earnings and growth of UWR after the merger and will not have any right to vote on corporate matters. Similarly, stockholders will not face the risk of losses generated by UWR's operations or decline in the value of UWR after the merger.

It is currently expected that, following the merger, the business and operations of UWR will generally continue as they are currently being conducted. LAH currently intends to cause UWR's operations to continue to be run and managed by, among others, UWR's existing executive officers, and expects that certain of the directors of UWR will continue to serve on the board of directors of UWR, although LAH intends to review the composition of the boards of directors (or similar governing bodies) of UWR and its subsidiaries and to cause the election to such boards of directors (or similar governing bodies) of certain of its representatives. LAH will continue to evaluate all aspects of the business, operations, capitalization and management of UWR prior to and after the consummation of the merger and will take such further actions as it deems appropriate under the circumstances then existing. LAH is evaluating potential acquisitions of other water and/or wastewater services businesses, with the participation of UWR where permitted by applicable confidentiality agreements and the Merger Agreement. These evaluations may lead to an extraordinary corporate transaction. However, there can be no assurance that any such transactions or acquisitions will occur.

Shares of UWR common stock are currently traded on the New York Stock Exchange. Following the consummation of the merger, UWR common stock will no longer be quoted on the New York Stock Exchange, and the registration of UWR common stock under the Exchange Act will be terminated. Accordingly, after the merger there will be no publicly traded equity securities of UWR outstanding, and UWR will no longer be required to file periodic reports with the Securities and Exchange Commission.

Following the merger, LAH expects that UWR's board of directors will review UWR's policy of declaring regular quarterly dividends and may modify the amount or the frequency of the dividends.

Following the merger, SLDE and LAH also expect to review the effect of the merger on the ownership structure of UWR, LAH and their affiliates and may simplify or otherwise modify the ownership of entities within the group.

Except as otherwise discussed in this proxy statement, LAH has no present plans or proposals that would result in any extraordinary corporate transaction, such as a merger, reorganization, liquidation involving UWR or any of its subsidiaries, or sale or transfer of a material amount of assets of UWR or any of its subsidiaries or in any other material changes to UWR's capitalization, dividend policy, corporate structure, business or composition of the board of directors or the management of UWR.

However, none of the above will affect existing non-LAH stockholders as they will no longer hold an equity interest in UWR after the effective time of the merger.

Background of the Merger

During the last several years, the UWR board explored the possibility of participating in the general consolidation in the United States water industry through a business combination with a similar sized water company or the acquisition of a smaller water company. The board also considered making acquisitions jointly with LAH. In both cases, the UWR board determined that the premium UWR would have to pay would make a significant transaction dilutive to its stockholders and would depress, rather than enhance, short and intermediate term stockholder value.

At the end of the second quarter of 1999, in light of recent water service industry business combinations and their potential impact on UWR, the UWR board began to consider, among other strategic alternatives, enhancing stockholder value through a business combination of its own with, or a sale to, a larger company. The board considered pursuing a sale to LAH, which already owned approximately 30% of UWR's shares, as well as a sale of UWR to, or a business combination with, other companies.

On June 10, 1999, Donald L. Correll, UWR's chairman and chief executive officer, met informally with certain UWR board members (specifically, Douglas W. Hawes, Jon F. Hanson and Lawrence R. Codey) without the board's LAH-affiliated members (specifically, Thierry Bourbie, Charles Chaumin and George Keane) to discuss both the option of a sale to LAH and alternatives to such a transaction. In order to explore such a path more fully, the board members present and Mr. Correll determined to hire a financial advisor and agreed that Mr. Correll would research and recommend a financial advisor to the board.

The members of the board present at the June 10, 1999 informal meeting and Mr. Correll agreed that Mr. Correll should meet with LAH and SLDE to inform LAH and SLDE of UWR's interest in pursuing opportunities for a business combination with LAH or other industry leaders. On June 21, 1999, Mr. Correll met with Gerard Mestrallet, President of the Executive Board and Chief Executive Officer of SLDE; Francois Jaclot, Executive Vice President and member of the Executive Board of SLDE; Philippe Brongniart, member of the Executive Board of SLDE and President of LAH; and Gerard Payen, Executive Vice President of the Water Division of SLDE, to inform them of UWR's interest.

The UWR board met on July 8, 1999. At that meeting, Mr. Correll recommended that the board retain Morgan Stanley & Co. Incorporated as its financial advisor because of its general reputation and recent water services industry experience conducting the auction of Aquarion Water Company, a water services utility. The LAH-affiliated members of the board were then excused and the remaining members of the board received a presentation from Morgan Stanley regarding the potential value to UWR stockholders of a business combination with, or a sale to, a larger industry participant, including a sale to LAH. At the July 8th meeting, the board, without its LAH-affiliated members, also received a presentation from its legal advisors, LeBoeuf, Lamb, Greene & MacRae, L.L.P. regarding the board's legal obligations in merger and acquisition transactions. The LAH-affiliated board members then re-joined the meeting and the entire board ratified the engagement of Morgan Stanley. The terms of Morgan Stanley's engagement were set out in a letter dated as of July 2, 1999.

In addition, during the July 8, 1999 board meeting, Mr. Correll and certain UWR directors without the board's LAH-affiliated members discussed with Morgan Stanley and UWR's legal advisors the desirability of pursuing a business combination with industry leaders other than LAH. In these discussions, Morgan Stanley provided the board with a range of values that Morgan Stanley believed UWR could expect to receive if the company was exposed to the market place. Mr. Correll, the members of the UWR board present, Morgan Stanley and UWR's legal advisors discussed the procedures that the company could follow in an auction of the company. They also discussed the possibility that an auction might result in a lower price for UWR stockholders than the price that might possibly be obtained in a negotiated transaction with LAH. This discussion focused on the possibility that the interest of third parties seeking to purchase UWR might be adversely affected by a combination of factors such as LAH's 30% ownership interest in UWR, LAH's rights under the Governance Agreement between LAH and UWR and LAH's (or its affiliates') interest in the joint ventures between UWR and LAH (or their affiliates).

Before the conclusion of the July 8 board meeting, the directors present instructed Mr. Correll to commence discussions with LAH to determine whether it would be possible to negotiate a transaction with LAH that was at least as favorable to UWR and its stockholders as could be expected to be achieved with an independent third party. The directors also indicated to Mr. Correll that if a satisfactory transaction could not be negotiated with LAH, they would consider the possibility of commencing negotiations with third parties through an auction or otherwise.

On July 12, 1999, Gerard Payen and Charles Chaumin, Senior Vice President for North America of the Water Division of SLDE, met with Mr. Correll, Michael C.J. Fallon, Vice President of United Water Management and Services Inc., and certain UWR directors to discuss the procedure for determining whether, among other strategic alternatives, a sale to LAH would be advantageous to both sides. Those present at the meeting determined that financial advisors for both companies should meet separately with each other. UWR's and LAH's financial advisors met on July 27, 1999 to discuss, among other possibilities, the terms of a possible transaction between UWR and LAH. This meeting was followed by a meeting of the executives of the two companies on July 28, 1999 to discuss the results of the meeting between the financial advisors. At each of these meetings, LAH was informed that if it appeared that satisfactory terms for a transaction could not be reached with LAH, UWR intended to consider the possibility of commencing discussions with other parties about a possible transaction.

On August 2, 1999 the board of UWR met again and reviewed the status of discussions between UWR and LAH. The LAH-affiliated board members were then excused and the remaining board members discussed whether it would be desirable to commence a formal auction of the company or approach other parties individually in order to obtain the best the price for the company's stockholders in a potential sale or business combination. The UWR board members present concluded that because of the complexities presented by an auction, an auction would not be in the best interests of the UWR stockholders if a transaction could be negotiated with LAH that resulted in stockholders receiving a price at least as high as the high-end of the range of potential prices that UWR's financial advisors believed could be achieved in an auction. The UWR board, with the LAH-affiliated board members abstaining, authorized management to continue discussions with LAH and also authorized management to commence discussions with parties other than LAH regarding possible strategic alternatives for UWR when, and as, management deemed appropriate.

Discussions between UWR and LAH continued throughout the first three weeks of August 1999. On August 18, 1999 in response to a significant increase in the trading values and volume of UWR stock, UWR announced that it was engaged in discussions regarding a possible business combination but did not name LAH. On August 18, 1999, SLDE released a statement indicating that its subsidiary, LAH, was discussing a possible business combination with UWR. Final agreement on the terms of a sale to LAH was reached on August 20, 1999.

At a special meeting held on August 20, 1999 the board of directors of UWR, without the participation of its LAH-affiliated members, reviewed and considered LAH's proposal. At this meeting, Morgan Stanley noted that, based on all measures that it believed relevant, the LAH offer provided more value, from a financial point of view, to UWR stockholders than any other recent, publicly announced transaction for acquisition of a comparable water services company. UWR's legal advisors also updated the UWR board on the terms of the proposed merger agreement with LAH and discussed other legal matters relating to the transaction.

Following the board's review of the LAH proposal, the LAH-affiliated members of the UWR board were invited to join the meeting. The offer by LAH to acquire the company was then approved by the unanimous vote of the UWR board with the LAH members abstaining and then by a second unanimous vote with the LAH members voting in favor of the transaction.

Reasons for the Merger and Recommendation of the UWR Board of Directors

UWR believes that the consideration to be paid in the merger exceeds the value for its stockholders that UWR would be able to achieve in the foreseeable future if UWR remained an independent company and exceeds the value that UWR stockholders would receive if UWR were able to sell to, or do a business combination with, a company other than LAH. As a result, the UWR board has unanimously (with its LAH-affiliated members first abstaining and then joining in that approval) approved the Merger Agreement and determined that the merger is advisable for, fair to and in the best interests of UWR stockholders other than LAH. The UWR board unanimously (with its LAH-affiliated members first abstaining and then joining in the recommendation) recommends that the stockholders of UWR vote **FOR** adoption of the Merger Agreement.

In determining that the merger maximizes stockholder value, the UWR board consulted with UWR's legal and financial advisors and considered a number of factors, including the following:

- The board's conclusion that UWR would not be able to achieve stockholder value equal to the purchase price being paid by LAH either through its current operations or through a business combination with a similar sized water company or acquisitions of smaller water companies. The UWR board believes that UWR is a well run company, and therefore, there is limited opportunity to greatly enhance stockholder value through simply continuing to operate its current businesses more efficiently or effectively. In light of the premiums being paid for acquisitions in the water industry, and UWR's experience through participation as a bidder in auctions of other water companies, the UWR board believes that the premium it would be required to pay to expand UWR through acquisitions would be dilutive to its stockholders and would depress stockholder value in the short and intermediate term. Furthermore, the UWR board is not convinced that in the long term, the strategy of acquisitions would necessarily result in a stock price that exceeds the price which could be achieved now through sale of the company to LAH.

- Based on advice from Morgan Stanley, UWR's own experience in participation in water company auctions and the consideration paid in publicly announced transactions involving water companies, the board's conclusion that the price to be paid by LAH in the merger exceeds the consideration that UWR stockholders could reasonably expect to receive in a transaction with another party.
- LAH's and SLDE's commitment to the United States water services business, as evidenced by SLDE's recent agreements to acquire Nalco Chemical Company and Calgon Corporation and the success of the United Water Services joint ventures with LAH, made it likely that LAH would pay as much or more for UWR than any other buyer.
- The uncertainty as to the effect that LAH's ownership of approximately 30% of UWR's shares of common stock and LAH's rights under its Governance Agreement with UWR and other agreements between LAH and UWR would have on the price a third party would be willing to bid for UWR. Pursuant to the terms of the Governance Agreement, UWR is required to provide LAH with 30 days' prior notice before it agrees to enter into a business combination with a third party. During that 30 day period, LAH has the right to make an offer to UWR for acquisition of UWR and the right to acquire additional UWR shares in the open market. The UWR board believes, after consultation with its financial and legal advisors, that LAH's share ownership in UWR and UWR's rights and obligations under the Governance Agreement and other agreements with LAH and its affiliates, such as the North American Rights Agreement between LAH, UWR and other parties, the partnership agreement relating to UWR's investment in the United Kingdom and agreements to provide water services in Canada, Mexico and the United States through joint venture companies in which LAH is part owner, could adversely affect the price that a third party bidder would be willing to pay for UWR.
- The written opinion of Morgan Stanley dated August 20, 1999 to the effect that, subject to, and based on, certain factors in its letter, the consideration to be paid to UWR stockholders in the merger was fair, from a financial point of view, to the holders of UWR common stock other than LAH and its affiliates.
- Discussions with Morgan Stanley at the August 20, 1999 board meeting that, based on relevant measures, the LAH offer exceeded the consideration paid in recent comparable transactions.
- The fact that the price of $35.00 per common share being paid by LAH, without regard to the increase in regular quarterly dividends which the UWR board has the right to and intends to pay in contemplation of the merger, represents a premium of approximately 52.3% over the $22.98 per share average closing price of UWR common stock for the 30 trading days immediately preceding UWR's announcement on August 18, 1999 that it was engaged in merger negotiations.
- The UWR board's assessment that LAH has the financial capability to consummate the merger and the agreement by SLDE to stand behind LAH's financial obligations under the Merger Agreement.
- The fact that the Merger Agreement requires the approval of two-thirds of UWR's common stockholders other than LAH, which allows for an informed vote of UWR's public stockholders on the transaction.
- The terms and conditions of the Merger Agreement, including those relating to the ability of the UWR board to consider unsolicited offers from third parties prior to approval of the Merger Agreement by UWR stockholders.

The UWR board of directors has also considered (1) the risk that the benefits sought in the merger would not be obtained, (2) the risk that the merger would not be consummated, (3) the effect of the public announcement of the merger on UWR's sales, customer and supplier relationships, operating results and ability to retain employees, and on the trading price of UWR common stock, (4) the substantial management time and effort that will be required to consummate the merger, (5) the impact of the merger on UWR employees, (6) the possibility that certain provisions of the Merger Agreement might have the effect of discouraging other persons potentially interested in a combination with UWR from pursuing such an opportunity and (7) other matters, including those described under "Forward Looking Statements". In the judgment of the UWR board of directors, the potential benefits of the merger outweigh these considerations.

The foregoing discussion of the information and factors considered by the board of directors is not intended to be exhaustive but is believed to include all material factors considered by the board of directors. In view of the variety of factors considered in connection with its evaluation of the merger, the board of directors did not find it practicable to, and did not, quantify or otherwise attempt to assign relative weight to the specific factors considered in reaching its determination. In addition, individual members of the board of directors may have given different weights to different factors. In the course of its deliberations, the board of directors did not establish a range of values for UWR; however, based on the factors outlined above, the board of directors, by a unanimous vote, with its LAH-affiliated members first abstaining and then joining in the vote, determined that the Merger Agreement and the merger are advisable for, fair to, and in the best interest of, UWR and its stockholders.

Opinion of UWR's Financial Advisor

On July 2, 1999, Morgan Stanley was engaged by UWR to provide financial advisory services and a financial fairness opinion with respect to the fairness, from a financial point of view, of the consideration to be received by the holders of shares of UWR common stock other than LAH and its affiliates. Morgan Stanley was selected by UWR's board of directors to act as UWR's financial advisor based on Morgan Stanley's general qualifications, expertise, reputation and its knowledge of the business and affairs of the water and wastewater services industry. At a meeting of UWR's board of directors on August 20, 1999, Morgan Stanley rendered its opinion, subsequently confirmed in writing, that as of August 20, 1999, and based upon and subject to the various considerations noted in the opinion, the consideration to be received by the holders of shares of UWR common stock pursuant to the Merger Agreement was fair, from a financial point of view, to the holders of shares of UWR common stock other than LAH and its affiliates. Morgan Stanley subsequently confirmed its opinion by delivering an updated opinion dated the date of this proxy statement.

The opinion of Morgan Stanley dated the date of this proxy statement, which sets forth, among other things, the assumptions made, procedures followed, matters considered and limitations on the scope of review undertaken by Morgan Stanley in rendering its opinion is attached as Annex B to this proxy statement. The opinion is substantially similar to the opinion of Morgan Stanley dated August 20, 1999. UWR stockholders are urged to, and should, read the opinion carefully and in its entirety. Morgan Stanley's opinions are directed to UWR's board of directors and addresses only the fairness from a financial point of view of the consideration to be received by the holders of shares of UWR common stock other than LAH and its affiliates pursuant to the Merger Agreement, as of the date of the opinion. Morgan Stanley's opinions do not address any other aspect of the merger and do not constitute a recommendation to any holder of UWR common stock as to how to vote at the UWR special meeting. The summary of the opinion of Morgan Stanley, which is set forth in this proxy statement is qualified in its entirety by reference to the full text of such opinion.

For purposes of its opinions, Morgan Stanley:

- reviewed certain publicly available financial statements and other information of UWR;
- reviewed certain internal financial statements and other financial and operating data concerning UWR prepared by the management of UWR;
- reviewed certain financial projections prepared by the management of UWR;
- discussed the past and current operations and financial condition and the prospects of UWR with senior executives of UWR;

- reviewed the pro forma impact of the merger on SLDE's earnings per share, consolidated capitalization and financial ratios;
- reviewed the reported prices and trading activity for UWR common stock;
- compared the financial performance of UWR and the prices and trading activity of UWR common stock with that of certain other comparable publicly-traded companies and their securities;
- reviewed the financial terms, to the extent publicly available, of certain comparable acquisition transactions;
- participated in discussions and negotiations among representatives of UWR, LAH and SLDE and their financial and legal advisors;
- reviewed certain material agreements between UWR and LAH;
- reviewed the draft Merger Agreement and certain related documents; and
- performed such other analyses and considered such other factors as Morgan Stanley deemed appropriate.

In rendering its opinions, Morgan Stanley assumed and relied upon, without independent verification, the accuracy and completeness of the information reviewed by it for the purposes of its opinions. With respect to the internal financial statements and other financial and operating data, including financial projections, Morgan Stanley assumed that they were reasonably prepared on bases reflecting the best currently available estimates and judgments of the prospects of UWR. In addition, Morgan Stanley assumed that the merger will be consummated in accordance with the terms set forth in the Merger Agreement. Morgan Stanley has not made any independent valuation or appraisal of the assets or liabilities of UWR. Morgan Stanley's opinions are necessarily based on financial, economic, market and other conditions as in effect on and the information made available to it as of the dates of its opinions.

The following is a brief summary of certain analyses performed by Morgan Stanley in connection with its opinion dated August 20, 1999. Certain of these summaries of financial analyses include information presented in a tabular format. In order fully to understand the financial analyses used by Morgan Stanley, the tables must be read together with the text of each summary. The tables alone do not constitute a complete description of the financial analyses.

Comparative Stock Price Performance. Morgan Stanley reviewed the recent stock price performance of UWR and compared such performance with that of the following indices:

- U.S. regulated water company index which included eight companies: American Water Works Company, Inc., Philadelphia Suburban Corporation, E'town Corporation, California Water Service Group, American States Water Company, SJW Corp., Connecticut Water Service, Inc. and Middlesex Water Company; and
- Standard & Poor's 500 Index.

The following table presents the change in the stock prices for these groups, as compared to the change in the stock prices of UWR common stock over the period from August 18, 1998 to August 18, 1999 and the period from May 18, 1999 to August 18, 1999.

	Percentage Change for the Period 8/18/98 to 8/18/99	Percentage Change for the Period 5/18/99 to 8/18/99
U.S. regulated water company index	21.7%	17.4%
Standard & Poor's 500 Index	21.0%	0.0%
UWR	57.9%	32.3%

Comparable Public Company Analysis. As part of its analysis, Morgan Stanley compared certain financial information of UWR with that of a group of publicly-traded regulated water companies, (collectively, the "UWR Comparable Companies"). The comparable companies selected for UWR were as follows:

UWR Comparable Companies

American States Water Company
American Water Works Company, Inc.
California Water Service Group
Connecticut Water Service, Inc.
E'town Corporation
Middlesex Water Company
Philadelphia Suburban Corporation
SJW Corp.

The table below presents, as of August 18, 1999, the representative range for each of the ratios of price to forecasted fiscal 1999 and 2000 earnings, stock price to tangible book value (value of UWR's equity plus the face amount of outstanding debt and preferred stock) as of June 30, 1999, and price to the latest twelve-month ("LTM") operating cash flow multiple, and the aggregate value to LTM EBITDA multiple and the aggregate value to LTM EBIT multiple. The earnings projections were based on earnings projections as reported by I/B/E/S International Inc., a provider of financial information, as of August 18, 1999. In the table below "LTM" means "lastest twelve-months", "EBITDA" means "earnings before interest, tax, depreciation and amortization" and "EBIT" means "earnings before interest and tax".

	Price to Forecasted 1999 Earnings	Price to Forecasted 2000 Earnings	Price to Tangible Book Value	Price to Operating Cash Flow	Aggregate Value to LTM EBITDA	Aggregate Value to LTM EBIT
UWR Comparable Companies...	18.0 - 19.0	17.5 - 18.5	1.8 - 2.0	10.5 - 11.5	10.0 - 11.0	13.0 - 14.0
UWR....................	18.0	17.1	2.2	11.1	11.1	15.4

No company utilized in the comparable public company analysis as a comparison is identical to UWR. In evaluating the companies, Morgan Stanley made judgments and assumptions with regard to industry performance, general business, economic, market and financial conditions and other matters, many of which are beyond the control of UWR, such as the impact of competition on the business of UWR and the industry generally, industry growth and the absence of any material adverse change in the financial condition and prospects of UWR or the industry or in the financial markets in general. Mathematical analysis (such as determining an average or a median) is not in itself a meaningful method of using comparable public company data. Based on this analysis, Morgan Stanley calculated per share values for UWR common stock ranging from $20.45 to $23.08. This range was also multiplied by a 40% control premium to determine a valuation range. Based on this premium, Morgan Stanley calculated per share equity values for UWR ranging from $28.64 to $32.32. Morgan Stanley noted that the unaffected closing per share price of UWR common stock on August 12, 1999 was $23.06.

Discounted Cash Flow Analysis. Morgan Stanley performed a discounted cash flow analysis of UWR's core utility business and real estate operations and multiple analyses for its stakes in the water services business and the Northumbrian Partnership. For UWR's core utility and real estate operations, Morgan Stanley's discounted cash flow analysis was based on certain financial projections provided by UWR's management for the period 1999 through 2009. Unlevered free cash flow was calculated as net income available to common stockholders plus the aggregate of preferred stock dividends, depreciation and amortization, deferred taxes, and other noncash expenses and after-tax net interest expense, less the sum of capital expenditures and investment in noncash working capital. Morgan Stanley calculated terminal values by applying a range of perpetual growth rate multiples to the unlevered free cash flow in fiscal 2009 and the cash-flow streams and terminal values were then discounted to the present using a range of discount rates representing an estimated range of the weighted average cost of capital for UWR. The range of discount rates utilized for the valuation of the core business was 5.50%-7.00%. The range of perpetual growth rates applied for this exercise was 1.0% to 2.0%.

For UWR's stake in the water services business, Morgan Stanley applied revenue multiples of 1.0x-2.0x to projected 1999 operating revenues of $154.3MM. For UWR's stake in the Northumbrian Partnership, Morgan Stanley examined a group of U.K. publicly-traded regulated water companies, (collectively, the "UK Comparable Companies"). The comparable companies selected for the Northumbrian Partnership were as follows:

UK Comparable Companies

Anglian Water plc
Thames Water plc
Kelda Group plc
Severn Trent plc
Pennon Group plc

The table below presents, as of August 18, 1999, the representative range for each of the ratios of price to tangible book value multiple as of March 31, 1998, and stock price to LTM operating cash flow multiple, and the aggregate value to LTM EBITDA and LTM EBIT multiples.

	Price to Tangible Book Value	Price to Operating Cash Flow	Aggregate Value to LTM EBITDA	Aggregate Value to LTM EBIT
UK Comparable Companies	1.1 - 1.3	5.0 - 6.0	7.5 - 8.5	10.5 - 11.5

Based on these analyses, Morgan Stanley calculated per share values for UWR ranging from $26.04 to $35.88.

Analysis of Selected Precedent Transactions. Using publicly available information, Morgan Stanley considered six announced or completed transactions in the regulated water industry, which were deemed to be comparable to the merger. These transactions included:

- Yorkshire Water plc's acquisition of Aquarion Company
- California Water Service Group's acquisition of Dominguez Services Corporation
- American Water Works Company Inc.'s acquisition of National Enterprises
- Enron Corp.'s acquisition of Wessex Water plc
- Philadelphia Suburban Corporation's acquisition of Consumers Water Company
- Nipsco Industries Inc.'s acquisition of IWC Resources Corp.

Morgan Stanley compared certain publicly available financial and market statistics of the above precedent transactions to the merger. The table below presents, as of August 18, 1999, the representative range for each of the ratios of price to those implied by LTM earnings multiple, and price to tangible book value multiple as of June 30, 1999, and the aggregate value to LTM EBITDA and LTM EBIT multiples.

	Price to LTM Earnings	Price to Tangible Book Value	Aggregate Value to LTM EBITDA	Aggregate Value to LTM EBIT
Precedent Transactions	23.0 - 34.0	2.4 - 3.2	10.0 - 13.0	13.5 - 18.5

Based on this analysis, Morgan Stanley calculated per share values for UWR ranging from $21.18 to $32.79.

No transaction utilized as a comparison in the analysis of the above selected precedent transactions is identical to the merger, and, accordingly, an analysis of the results of the foregoing necessarily involves complex considerations and judgments concerning differences in financial and operating characteristics of UWR and other factors that would affect the acquisition value of the companies to which it is being compared. In evaluating the above precedent transactions, Morgan Stanley made judgments and assumptions with regard to industry performance, general business, economic, market and financial conditions and other matters, many of which are beyond the control of UWR, such as the impact of competition on UWR and the industry generally, industry growth and the absence of any adverse material change in the financial conditions and prospects of UWR or the industry or in the financial markets in general. Mathematical analysis (such as determining the mean or median) is not, in itself, a meaningful method of using precedent transactions data.

Pro Forma Analysis of the Merger. Morgan Stanley reviewed the pro forma impact of the merger on SLDE's earnings per share (''EPS'') for the fiscal years ended 2000 through 2004. The analysis was performed assuming completion of the merger at the beginning of this period, utilizing stand-alone I/B/E/S earnings estimated for the fiscal years ended 2000 through 2004 for UWR and SLDE prior to the inclusion of any synergies. Based on such analysis on an EPS basis, the merger would be dilutive post-goodwill to SLDE for the period 2000 through 2004 and accretive pre-goodwill in 2000, dilutive in 2001 and accretive for the period 2002 through 2004.

In connection with its opinion dated the date of this proxy statement, Morgan Stanley reviewed its analysis used to render its August 20, 1999 opinion by performing procedures to update certain analyses and by reviewing the assumptions upon which such analyses were based and the factors considered in connection with the August 20, 1999 opinion.

In connection with the review of the merger by UWR's board of directors, Morgan Stanley performed a variety of financial and comparative analyses for purposes of giving its fairness opinion. The preparation of a fairness opinion is a complex process and is not necessarily susceptible to partial analysis or summary description. In arriving at its opinions, Morgan Stanley considered the results of all of its analyses as a whole and did not attribute any particular weight to any analysis or factor considered by it. Furthermore, Morgan Stanley believes that selecting any portion of its analyses, without considering all analyses, would create an incomplete view of the process underlying its opinions. In addition, Morgan Stanley may have given various analyses and factors more or less weight than other analyses and factors, and may have deemed various assumptions more or less probable than other assumptions, so that the ranges of valuations resulting from any particular analysis described above should not be taken to be Morgan Stanley's view of the actual value of UWR.

In performing its analyses, Morgan Stanley made numerous assumptions with respect to industry performance, general business and economic conditions and other matters, many of which are beyond the control of UWR and SLDE. Any estimates contained in Morgan Stanley's analysis are not necessarily indicative of future results or actual values, which may be significantly more or less favorable than those suggested by such estimates. The analyses performed were performed solely as part of Morgan Stanley's analysis of the fairness, from a financial point of view, of the consideration to be received by the holders of shares of UWR common stock, other than LAH and its affiliates, pursuant to the Merger Agreement and were conducted in connection with the delivery of the Morgan Stanley opinions dated August 20, 1999 and dated the date of this proxy statement to UWR's board of directors. The analyses do not purport to be appraisals or to reflect the prices at which UWR common stock might actually trade. The consideration pursuant to the Merger Agreement and other terms of the Merger Agreement were determined through arm's length negotiations between UWR and SLDE and were approved by UWR's board of directors. Morgan Stanley provided advice to UWR during such negotiations; however, Morgan Stanley did not recommend any specific consideration to UWR or that any specific consideration constituted the only appropriate consideration for the merger. In arriving at its opinions, Morgan Stanley was not authorized to solicit, and did not solicit, interest from any party with respect to the acquisition of UWR or any of its assets, nor did Morgan Stanley negotiate with any parties, other than LAH and SLDE. Morgan Stanley's opinion dated August 20, 1999 was one of many factors taken into consideration by UWR's board of directors in making its decision to approve the Merger Agreement and the transactions contemplated by it. Consequently, the Morgan Stanley analyses described above should not be viewed as determinate of the opinion of UWR's board of directors with respect to the value of UWR or to whether or not the UWR board of directors would have been willing to agree to a different consideration.

UWR's board of directors retained Morgan Stanley based upon Morgan Stanley's qualifications, experience and expertise. Morgan Stanley is an internationally recognized investment banking and advisory firm. Morgan Stanley, as part of its investment banking and financial advisory business, is continuously involved in the valuation of businesses and securities in connection with mergers and acquisitions, negotiated underwritings, competitive biddings, secondary distributions of listed and unlisted securities, private placements and valuations for corporate and other purposes. In the ordinary course of Morgan Stanley's trading and brokerage activities, Morgan Stanley or its affiliates may at any time hold long or short positions, may trade or otherwise effect transactions for its own account or for the account of customers in the equity or debt securities of UWR or SLDE.

Morgan Stanley has been retained by UWR to act as financial advisor to UWR with respect to the merger. Pursuant to a letter agreement dated July 2, 1999 between UWR and Morgan Stanley, Morgan Stanley is entitled to (i) an advisory fee of approximately $50,000 to $100,000 which is payable in the event the transaction is not consummated and (ii) a transaction fee equal to approximately $6,000,000, which is payable as follows: one-third upon announcement of the transaction, one-third upon approval of the transaction by UWR stockholders and one-third upon closing of the transaction. Any amounts paid or payable to Morgan Stanley as advisory or announcement fees will be credited against the transaction fee. UWR has also agreed to reimburse Morgan Stanley for its expenses in performing its services. In addition, UWR has agreed to indemnify Morgan Stanley and its affiliates, their respective directors, officers, agents and each person, if any, controlling Morgan Stanley or any of its affiliates against certain liabilities and expenses, including certain liabilities under the federal securities laws, related to or arising out of Morgan Stanley's engagement and any related transactions. In the past, Morgan Stanley & Co. Incorporated and its affiliates have provided financial advisory and financing services for SLDE and have received fees for the rendering of these services.

Financial Projections of UWR

Following are certain financial projections provided by UWR management to its board of directors including its LAH-affiliated members at its July 8, 1999 meeting. The projections were subsequently provided to Rothschild Inc. and Morgan Stanley. The projected results for fiscal year 1999 set forth in the projections were based upon actual results through March 1999 and management forecasts for the remainder of fiscal 1999.

UWR Consolidated Statement of Income

Years Ended December 31, 1998–2003
(thousands of dollars)

	Actual	Projected				
	1998	1999	2000	2001	2002	2003
Operating revenues	$356,210	$367,040	$364,503	$379,361	$396,693	$408,516
Operating expenses and taxes						
Operations	147,090	153,322	139,909	145,087	150,153	153,099
Maintenance	21,297	22,538	22,476	22,487	22,463	22,403
Depreciation	39,950	44,491	41,771	43,367	44,539	45,502
General taxes	50,273	54,784	53,541	54,707	56,188	57,644
Total operating expenses and taxes	258,610	275,135	257,697	265,647	273,343	278,649
Operating income	97,600	91,905	106,806	113,714	123,350	129,867
Other income						
Investments, acquisitions & divestments (net of tax)	—	5,894	8,255	9,165	9,263	8,645
AFUDC	4,567	2,289	3,142	1,950	1,733	1,722
Other, (net)	1,959	7,962	366	51	2	21
Equity earnings (net of interest expense)	6,491	6,940	3,228	5,012	5,077	8,920
Total other income	13,017	23,085	14,990	16,178	16,075	19,308
Gross Income	110,617	114,990	121,796	129,892	139,424	149,175
Interest and other charges						
Interest on long-term debt & amortization	36,036	39,521	35,223	35,547	36,113	36,037
Other interest expense	4,921	4,749	5,935	6,405	6,537	6,248
Total interest & other charges	40,957	44,270	41,158	41,953	42,649	42,285
Profit before taxes & preferred dividends	69,660	70,720	80,638	87,939	96,775	106,890
Provision for income taxes	19,450	18,799	23,502	26,251	29,918	33,683
Net Income	50,210	51,921	57,136	61,688	66,857	73,207
Preferred and preference stock dividends	6,281	4,886	2,867	2,143	1,841	1,537
Net income applied to common stock	$ 43,929	$ 47,035	$ 54,269	$ 59,545	$ 65,016	$ 71,670
Average shares outstanding	37,028	38,578	39,331	39,854	40,379	41,178
Earnings per share	$1.19	$1.22	$1.38	$1.49	$1.61	$1.74

UWR does not, as a matter of course, make public its forecasts or projections as to the future sales, earnings or other income statement data, cash flows or balance sheet and financial position information. The above summary of these projections is included in this proxy statement solely because the projections were made available to LAH and its affiliates and Morgan Stanley. The projections do not reflect any of the effects of the merger or other future adjustments that may be appropriate concerning UWR and its assets, business, operations, properties, policies, corporate structure, capitalization and management in light of the circumstances then existing.

During the period from July 8 through August 20, 1999, Morgan Stanley conducted diligence on UWR and its affiliates and discussed various aspects of UWR's business with its management. Based on these discussions, an adjusted set of projections was prepared. For UWR's core utility business and real estate operations, Morgan Stanley's discounted cash flow analysis was based on the adjusted projections. These adjusted projections differed from those dated as of July 8, 1999, generally, in that the adjusted projections were extended through the year 2009, they included updated information regarding projected operating revenues and operating income (which did not differ materially from the amounts included in the projections dated as of July 8, 1999) and they eliminated anticipated income from investments, acquisitions and divestments that was considered speculative.

Other than as described above, UWR has not updated the projections to reflect changes that have occurred since their preparation. UWR believes the assumptions were reasonable at the time the projections were prepared, given the information known by its management at such time.

UWR did not prepare the projections with a view toward public disclosure or compliance with published guidelines of the Securities and Exchange Commission or the American Institute of Certified Public Accountants regarding forward looking information or generally accepted accounting principles. UWR's independent auditors, have not, and other independent accountants have not, compiled, examined or performed any procedure with respect to the prospective financial information contained in the projections, and they have not expressed any opinion or given any form of assurance on the projections or their achievability, and assume no responsibility for and disclaim any association with, such prospective information. Furthermore the projections necessarily make numerous assumptions, many of which are beyond the control of UWR and may not prove to have been and may no longer be accurate. Additionally, this information does not reflect revised prospects for UWR's businesses, changes in the general business and economic conditions, or any other transaction or event that has occurred or that may occur and that was not anticipated at the time the projections were prepared. Accordingly, the projections are not necessarily indicative of current value or future performance, which may be significantly more favorable or less favorable than described below, and should not be regarded as a representation that they will be achieved.

THE PROJECTIONS ARE NOT GUARANTEES OF PERFORMANCE. THEY INVOLVE RISKS, UNCERTAINTIES AND ASSUMPTIONS. THE FUTURE RESULTS OF UWR AND UWR'S VALUE MAY MATERIALLY DIFFER FROM THE PROJECTIONS. MANY OF THE FACTORS THAT WILL DETERMINE THESE RESULTS AND VALUES ARE BEYOND UWR'S ABILITY TO CONTROL OR PREDICT. HOLDERS OF THE COMMON STOCK ARE CAUTIONED NOT TO PLACE UNDUE RELIANCE ON THE PROJECTIONS. THERE CAN BE NO ASSURANCE THAT THE PROJECTIONS WILL BE REALIZED OR THAT UWR'S FUTURE FINANCIAL RESULTS WILL NOT MATERIALLY VARY FROM THE PROJECTIONS. UWR DOES NOT INTEND TO UPDATE OR REVISE THE PROJECTIONS.

SLDE's and LAH's Belief That The Merger is Fair To UWR's Unaffiliated Stockholders

Each of SLDE, LAH and LAH Acquisition reasonably believes that the merger is fair to UWR's unaffiliated stockholders. This belief is based on, among other things, SLDE's and LAH's experience in owning, managing, operating and divesting water companies, including water companies in the United States, and on its experience as a stockholder of UWR and as a joint venture partner with UWR in United Water Services. This view is also based on the fact that the terms and conditions of the merger, including the amount of the consideration to be paid to UWR's unaffiliated stockholders, were arrived at through arm's length negotiations between LAH and independent representatives of UWR. This belief is further supported by the understanding of SLDE, LAH and LAH Acquisition, based on discussions with and advice from their financial advisor, Rothschild Inc., as well as other publicly available information, that the consideration that the unaffiliated UWR stockholders will receive in the merger is at least equivalent to the consideration paid by the acquirers in other recent acquisitions of United States water companies, measured by relevant valuation methods, and represents a substantial premium over the market price of their shares prior to the announcement of the merger discussions between UWR and LAH. No director of SLDE, LAH or LAH Acquisition dissented to or abstained from voting on the merger.

Rothschild as Financial Advisor to SLDE and LAH

Rothschild Inc. has served as financial advisor to SLDE and its wholly-owned subsidiary LAH with respect to certain strategic alternatives regarding LAH's investment in UWR. SLDE did not request that Rothschild provide any opinion as to the fairness of the consideration to be received by holders of shares of UWR common stock pursuant to the Merger Agreement. In addition, although Rothschild, as financial advisor to SLDE and LAH, provided SLDE and LAH with advice as to the amount of consideration to be paid by LAH in the merger, SLDE did not request that Rothschild make any recommendation to the supervisory board of SLDE in this regard, the amount of consideration to be paid by LAH in the merger having been determined by SLDE's and LAH's senior management, in consultation with Rothschild, through active negotiations with UWR.

In connection with its role as financial advisor, Rothschild, among other things: (i) analyzed certain publicly available historical financial statements and other historical information concerning UWR prepared by UWR; (ii) reviewed the recent reported prices and trading activity for the common stock of UWR; (iii) compared the financial performance of UWR and the prices and trading activity of the common stock of UWR with that of certain other comparable publicly traded companies and their securities; (iv) reviewed certain financial projections for UWR that were based on both publicly available information and confidential information prepared by UWR for its board, which includes certain LAH-affiliated members, and which UWR made available to Rothschild, including details of estimated and forecasted operating and financial performance of UWR; (v) reviewed the terms of precedent transactions deemed relevant by Rothschild, to the extent publicly available; (vi) reviewed the Merger Agreement, and certain related documents; and (vii) conducted such other studies and analyses as it deemed appropriate. Rothschild did not assume any responsibility for conducting a physical inspection of the properties or facilities of UWR or for making or obtaining any independent valuation or appraisal of the assets or liabilities of UWR nor was Rothschild furnished with any such appraisals.

The following is a brief summary of the material financial and comparative analyses Rothschild performed in connection with its advice to SLDE and LAH.

Comparable Publicly Traded Companies Analysis of UWR. Rothschild reviewed and compared certain actual and projected financial, operating and stock market information of companies in lines of business Rothschild believed to be comparable to those of UWR. While there were no public companies with precisely the same mix of business and financial condition as UWR, Rothschild believed the most relevant comparable companies to UWR to be American Water Works Corporation, Inc., Philadelphia Suburban Corporation, E' Town Company, Middlesex Water Company and Connecticut Water Services, Inc. (for the purpose of this section, the "Comparable Companies"). The results of Rothschild's analysis are set forth below. For the purposes of this section, Enterprise Value means equity market value (based on the closing market prices of the Comparable Companies for the 12 months ending on August 17, 1999) plus net debt. EBITDA means earnings before interest, taxes, depreciation and interest. EBIT means earnings before interest and taxes; and LTM means latest twelve-months.

Summary of Comparable Companies Analysis

Multiple	Range
Enterprise Value as a multiple of LTM revenues	4.42x – 5.34x
Enterprise Value as a multiple of LTM EBITDA	9.7x – 12.6x
Enterprise Value as a multiple of LTM EBIT	13.1x – 16.6x
Market value as a multiple of LTM net income	16.8x – 25.0x
Price as a multiple of estimated 1999 earnings per share	17.6x – 21.5x
Price as a multiple of estimated 2000 earnings per share	16.7x – 18.4x
Market value as a multiple of book value	1.84x – 2.53x

Based on the foregoing data, other data deemed relevant for the Comparable Companies and the projections for UWR prepared by the management of UWR for its board, Rothschild performed a public market valuation analysis. Assuming a 30% change of control premium, this analysis indicated equity value reference ranges of approximately \$31.19 to \$35.87 for each share of UWR common stock. As noted above, no company used in the public market valuation analysis is comparable to UWR. Accordingly, any analysis of the value of the shares of UWR common stock based on the Comparable Companies involves complex considerations and judgments concerning differences in potential financial and operating characteristics of the Comparable Companies and other factors in relation to the trading and acquisition values of the Comparable Companies.

Selected Precedent Transaction Analysis. Rothschild reviewed and analyzed publicly available financial information relating to selected announced or completed merger and acquisition transactions in the regulated water industry between September 1996 and June 1999 (for the purposes of this section, the "Water Industry Transactions"). Rothschild believes that the reasons for, and the circumstances surrounding, each of the transactions analyzed were diverse and the characteristics of such transactions involved were not directly comparable to the merger or to UWR and that the merger and acquisition transactions environment varies over time because of macroeconomic factors such as interest rate and equity market fluctuations and microeconomic factors such as industry results and growth expectations.

Based on the Water Industry Transactions and the operating projections for UWR prepared by the management of UWR for its board, this analysis indicated implied equity value reference ranges of approximately \$32.39 to \$35.39 per share of UWR common stock. As noted above, no transaction reviewed was identical to the merger and, accordingly, an assessment of the results of this analysis necessarily involves complex considerations and judgments concerning differences in financial and operating characteristics of UWR and other factors that would effect the acquisition value of the companies to which UWR was compared.

Discounted Cash Flow Analysis of UWR. Based upon the projections for UWR prepared by the management of UWR for its board, Rothschild considered that the net present value of UWR's future consolidated cash flows and the present value of the implied terminal value less net UWR debt indicated net present values per share of UWR common stock ranging from approximately $33.02 to $38.95 on the basis of mid-range assumptions of discount rates of 6.75% to 7.25% and a 2008 perpetuity growth rate of 3%.

Average Acquisition Premium Analysis. Rothschild analyzed the implied consideration per share of UWR common stock based on the levels of premiums paid in selected acquisition transactions (for purposes of this section, the "Selected Transactions"). Rothschild believes that the reasons for, and circumstances surrounding, each of the transactions analyzed were diverse and the characteristics of such transactions and the companies involved were not directly comparable to the merger or to UWR. Based on average premiums in Selected Transactions ranging from 25% to 40%, in each case in relation to trading prices on the trading day immediately prior to the respective public announcements of such selected transactions, this analysis indicated a value per share of UWR common stock ranging from $28.72 to $32.15 based on a 30 day average closing price of $22.98 for the UWR common stock as of the date prior to the announcement by UWR that it was considering strategic alternatives.

"Sum-of-the-Parts" Analysis for UWR. Rothschild also considered a pre-tax "sum-of-the-parts" analysis for each segment of UWR. The segments analyzed were as follows:

- UWR's water utility business
- UWR's equity investment in the Northumbrian Partnership
- UWR's equity investment in the United Water Services joint ventures
- UWR's real estate operations and other investments

Summary of Sum-of-the-Parts Analysis

	Per Share Value	
	Low	**High**
Water Utility Business	$30.20	$32.96
Investment in Northumbrian Partnership	$ 2.83	$ 3.27
Investment in United Water Services	$ 1.68	$ 2.16
Real Estate and Other Investments	$ 2.16	$ 2.40
Less UWR debt	$ (3.69)	$ (3.69)
Sum-of-the-Parts Value	$33.18	$37.10

In connection with its role as financial advisor to SLDE, Rothschild analyzed various other strategic options available with respect to LAH's stake in UWR, including the sale of its stake to a strategic buyer, renegotiating the agreements that govern the relationship between UWR and LAH and SLDE, and maintaining the status quo.

Rothschild's analyses were based on information then available and the best economic assumptions available to it at that time and various other factors. Rothschild's views do not constitute an opinion as to a fair valuation of UWR or the shares of UWR common stock, or the optimum price to be achieved by the stockholders of UWR, nor do Rothschild's analyses purport to be a comprehensive review of all options available to UWR. Since Rothschild's views described above are inherently subject to uncertainty, none of SLDE, LAH, Rothschild or any other person assumes responsibility for their accuracy or for reliance by any stockholder of UWR upon them.

SLDE retained Rothschild to act as its advisor based upon Rothschild's qualifications, experience and expertise. Rothschild is an internationally recognized investment banking firm and, as a part of its investment banking business, is engaged in the rendering of merger and acquisition advice, the valuation of businesses and their securities in connection with mergers and acquisitions, negotiated underwritings, private placements and valuations for corporate and other purposes. Rothschild may actively trade the equity securities of UWR for its own account and for the account of its customers and, accordingly, may at any time hold a long or short position in such securities.

Except as described herein, neither SLDE nor LAH has obtained, or sought to obtain, any report, opinion or appraisal from an outside party.

Potential Conflicts of Interest of Certain Persons in the Merger

In considering the recommendation of UWR's board of directors with respect to the Merger Agreement, stockholders should be aware that certain directors and executive officers of UWR have interests that may present them with potential conflicts of interest in connection with the merger. UWR's board of directors is aware of the conflicts described below and considered them along with other matters in recommending that UWR stockholders vote to approve the Merger Agreement.

UWR has issued to certain of its directors and executive officers options to purchase shares of UWR common stock under its Management Incentive Plan and shares of restricted common stock under its Directors' Restricted Stock Plans. At the effective time of the merger, all holders of options to purchase UWR common stock, will receive in exchange for the cancellation of their options a cash payment per share equal to the excess of $35.00 over the applicable exercise price. In addition, each outstanding share of restricted common stock issued under the Directors' Restricted Stock Plans will become fully vested at the effective time of the merger and will be simultaneously converted into the right to receive a cash payment of $35.00 per share.

Approval of the merger by shareholders of UWR will constitute a change of control of UWR under the employment agreements between UWR and several UWR executive officers, including Messrs. Correll, Simunovich, DeMicco, McGlynn, and Fallon. The exact terms of the employment agreements vary. Generally, however, the agreements entitle the executives to severance payments and benefits if, following a change of control, UWR terminates the executive's employment for other than cause or if the executive terminates employment for good reason. Cause is generally defined in the agreements to include actions, such as the executive's failure to perform his or her duties, the willful engaging of the executive in misconduct, or the executive's conviction of a felony, if such actions would cause material injury to UWR. Good reason is defined in the agreements to include, among other things, a reduction in the executive's base salary, an adverse change in the executive's duties or responsibilities, and, in all but one of the agreements, a change of the executive's place of employment to one that is more than 50 miles from where the executive is currently working. Additionally, Mr. Correll's agreement provides that severance payments and benefits will be paid following a termination or resignation for any reason during the six month period following the consummation of a transaction that constitutes a change of control and the agreements of Messrs. Simunovich, DeMicco and Fallon provide that severance payments and benefits will be paid following a termination or resignation for any reason during the thirteenth month following the consummation of a transaction that constitutes a change of control. Severance benefits provided under the agreements include the following:

- a payment equal to two or three hundred percent of the executive's annual base salary and annual target bonus;
- continued participation for 18 or 24 months in employee benefit plans in which the executive is entitled to participate, or the cash equivalent if continued participation is not possible; and
- payment of the executive's nonqualified supplemental retirement plan benefit, assuming for purposes of determining the benefit that it is fully vested, and that the executive has attained at least age 55 with at least 10 years of service under the plan.

The agreements also provide for an additional payment, if required, to make the executives whole for any excise tax imposed by Section 4999 of the Internal Revenue Code.

It is presently estimated that the value of the severance payments and benefits, including the excise tax gross-up payments, to which the named executive officers would become entitled under their employment agreements, assuming for this purpose that each executive's employment was terminated for one of the reasons set forth above following UWR shareholder approval of the merger, would be as follows: Mr. Correll, $4,343,000; Mr. Simunovich, $2,120,000; Mr. DeMicco, $1,880,000; Mr. McGlynn, $700,000; and Mr. Fallon, $1,880,000.

Indemnification and Insurance

The Merger Agreement provides that after the effective time of the merger, LAH, and UWR will, to the fullest extent permitted by applicable law, indemnify each of the past and present officers and directors of the parties and their subsidiaries, as well as anyone who becomes an officer or director after the date of the Merger Agreement but prior to the effective time, against:

- liabilities and expenses (including attorneys' fees) arising out of actions or omissions by such person at or prior to the effective time of the merger and based on the fact that such person is or was a director or officer of a party to the Merger Agreement or one of their subsidiaries; and
- all such liabilities to the extent they arise out of the Merger Agreement.

LAH is also required to maintain directors' and officers' liability insurance policies for six years following the effective time of the merger for the benefit of the persons currently covered by such policies of UWR or its subsidiaries, although LAH is not, however, required to spend in any year more than 200% of the annual aggregate premiums currently paid by UWR for such insurance.

Federal Income Tax Consequences

The receipt of cash by each holder of shares of common stock and series A preference stock pursuant to the Merger Agreement will be a taxable transaction for U.S. federal income tax purposes and may also be a taxable transaction under applicable state, local, foreign and other tax laws.

Generally, a stockholder of UWR who receives cash in exchange for shares of UWR common stock or series A preference stock pursuant to the merger will, for U.S. federal income tax purposes, recognize gain or loss equal to the difference between the amount of cash received and such stockholder's adjusted tax basis in the UWR common stock or series A preference stock exchanged. If the UWR common stock or series A preference stock is held by a stockholder as a capital asset, gain or loss recognized by the stockholder will be a long-term capital gain or loss if the stockholder has held the common stock for more than one year. In the case of a noncorporate taxpayer, the current maximum U.S. federal income tax rate on net capital gains generally is 20%.

Payments of cash to a holder of shares of UWR common stock or series A preference stock are generally subject to information reporting requirements. "Backup" withholding at a rate of 31% will apply to such payments, unless the holder furnishes its taxpayer identification number in the manner prescribed in the applicable U.S. Treasury regulations, certifies that such number is correct, certifies as to no loss of exemption from backup withholding and meets certain other conditions. Any amounts withheld under the backup withholding rules will be allowed as a refund or credit against the holder's U.S. federal income tax liability if the required information is furnished to the Internal Revenue Service. Such "backup" withholding can be avoided if a stockholder properly completes the letter of transmittal that the exchange agent will mail to each stockholder as soon as reasonably practicable after the effective time of the merger, and includes in such letter the stockholder's correct taxpayer identification number.

The discussion set forth above as to the material federal income tax consequences of the merger is based upon the provisions of the Internal Revenue Code of 1986, as amended, applicable U.S. Treasury regulations, judicial decisions and current administrative rulings, all as in effect on the date of this proxy statement and all of which are subject to change at any time possibly with retroactive effect. This discussion does not address any aspect of state, local or foreign taxation. No rulings have been, or will be, requested from the Internal Revenue Service with respect to any of the matters discussed. There can be no assurance that future legislation, regulations, administrative rulings or court decisions will not alter the tax consequences described above.

This discussion does not purport to be a complete analysis or discussion of all potential tax effects relevant to the merger. The foregoing discussion may not be applicable with respect to certain shares received pursuant to the exercise of employee stock options or otherwise as compensation or with respect

to holders of shares who are subject to special tax treatment under the U.S. Internal Revenue Code of 1986, as amended, such as non-U.S. persons, life insurance companies, tax-exempt organizations and financial institutions, and may not apply to a holder of shares in light of that holder's individual circumstances. Stockholders are urged to consult their own tax advisers to determine the particular tax consequences of the merger to them (including the application and effect of any state, local or foreign income and other tax laws) of the merger.

Regulatory Matters

UWR has public utility subsidiaries which operate in thirteen states. While certain of the relevant state statutes are subject to interpretation regarding their applicability to this transaction, UWR believes that approvals of the state public utility regulatory commissions in at least ten states are required. These 10 states are Arkansas, Connecticut, Delaware, Florida, Illinois, Missouri, New Jersey, New York, Pennsylvania and Virginia. Filings for such approvals are expected to be made during the month of October 1999. The Merger Agreement requires UWR to use all commercially reasonable efforts to obtain the necessary approvals as soon as practicable. While there can be no guarantee as to whether or when these approvals will be finally obtained, UWR believes that all approvals will be received during the first half of the year 2000.

Antitrust Regulation. Under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, and the related rules promulgated by the Federal Trade Commission, the merger may not be consummated until notifications have been given and certain information has been furnished to the Federal Trade Commission and the Antitrust Division of the Department of Justice and the applicable waiting period requirement has expired or been terminated. Each of UWR and LAH expects to file a notification and report form under the Hart-Scott-Rodino Act before December 31, 1999. The waiting period under the Hart-Scott-Rodino Act will expire 30 days after these filings unless early termination is granted by the Federal Trade Commission and the Department of Justice or additional information is requested by them from either UWR or LAH. If the merger is not consummated within one year after the expiration of the Hart-Scott-Rodino Act waiting period, UWR and LAH will be required to re-file under the Hart-Scott-Rodino Act. Satisfaction of the waiting period requirement does not preclude the Department of Justice, the Federal Trade Commission or any other party from challenging or seeking to delay or enjoin the merger on antitrust or other grounds either before or after the effective time. There can be no assurance that such a challenge, if made, would not be successful. UWR and LAH believe that the merger would not violate federal antitrust laws.

Absence of Appraisal Rights

The stockholders of UWR are not entitled to appraisal rights in connection with the merger. Under New Jersey law, an appraisal right is the right to dissent from the merger and obtain payment of an appraised value for your shares in place of the cash consideration payable in the merger.

Recent Developments

As of the date of this proxy statement, two law suits have been filed contesting the merger. These suits are (1) *Herbert Behrens v. Donald L. Correll et al.*, filed on August 25, 1999 in the Superior Court of New Jersey Chancery Division, Bergen County, Docket No. C-260-99, and (2) *Lawrence Steinberg v. United Water Resources Inc. et al.*, filed on August 24, 1999 in the Superior Court of New Jersey Chancery Division, Bergen County, Docket No. C-256-99.

These suits allege, among other things, breach of fiduciary duty by UWR and its directors because the merger was purportedly agreed to without an appropriate evaluation of UWR's worth to an acquisition candidate. Both suits seek, in addition to other relief, an injunction preventing SLDE and LAH from acquiring UWR for the consideration stated in the Merger Agreement.

UWR believes that these suits are entirely without merit and intends to vigorously defend against them.

THE MERGER AGREEMENT

The following is a description of certain provisions of the Merger Agreement. The complete Merger Agreement appears as Annex A to this proxy statement and is incorporated herein by reference. This description does not purport to be complete and it may not include all of the information that interests you. The description is qualified in its entirety by reference to the Merger Agreement, and we recommend that you carefully read the Merger Agreement in its entirety.

Effective Time of the Merger

The merger will take place only after receipt of all necessary stockholder and regulatory approvals and the satisfaction or waiver of the conditions to the merger. As required by the Merger Agreement, the parties must also file a certificate of merger with the Secretary of State of New Jersey before the merger can take effect. The merger will take effect at such time as the certificate of merger is duly filed with the Secretary of State of New Jersey, or on a subsequent date that the parties agree to and specify in the certificate of merger.

Effects of the Merger

At the effective time of the merger, LAH Acquisition will merge with and into UWR and UWR will be the surviving corporation. At such time, the separate corporate existence of LAH Acquisition will cease, and UWR will become a wholly-owned subsidiary of LAH.

The certificate of incorporation and by-laws of LAH Acquisition, immediately prior to the effective time of the merger, will be the certificate of incorporation and by-laws of UWR following the merger. The directors of LAH Acquisition and the officers of UWR, immediately prior to the effective time of the merger, will be the directors and officers of UWR following the merger.

The other effects of the merger will be as provided in the applicable provisions of the New Jersey Business Corporation Act.

Merger Consideration

The Merger Agreement reflects an "all-cash transaction" in which each issued and outstanding share of UWR common stock (other than shares owned, directly or indirectly, by UWR, LAH or any of their respective wholly-owned subsidiaries) will be converted at the effective time of the merger into the right to receive the per share cash consideration of $35.00, without interest. Each issued and outstanding share of series A preference stock (other than shares owned, directly or indirectly, by UWR, LAH or any of their respective wholly-owned subsidiaries) will be converted into a right to receive $29.17 in cash. This amount is equal to the product of $35.00 multiplied by the 0.8333 shares of common stock into which each share of series A preference stock is convertible immediately prior to the effective time of the merger. All shares of common stock and series A preference stock owned, directly or indirectly, by UWR or LAH or any of their respective wholly-owned subsidiaries will be canceled without consideration in the merger.

Exchange of Stock Certificates

Exchange Agent. Prior to the effective time of the merger, LAH will enter into an agreement with a bank or trust company mutually acceptable to UWR and LAH to serve as an exchange agent for the merger. At the effective time of the merger, LAH will deposit cash with the exchange agent in an amount equal to:

- the aggregate cash consideration payable to all eligible holders of UWR common stock and series A preference stock under the Merger Agreement; plus
- the aggregate amount of any dividends on UWR common stock and series A preference stock that have been declared but remain unpaid at the effective time of the merger.

Exchange Procedures. Promptly after the effective time, LAH and UWR will cause the exchange agent to mail the following materials to each person, other than UWR, LAH and their wholly-owned subsidiaries, who at the effective time held a certificate or certificates representing outstanding shares of UWR common stock or series A preference stock:

- a letter of transmittal for use in submitting such share certificate to the exchange agent for exchange; and
- instructions explaining what the stockholder must do to receive the per share cash consideration in exchange for surrender of their share certificates.

Upon surrender of a share certificate to the exchange agent for cancellation, the holder of the certificate shall be entitled to receive in exchange therefor the per share cash consideration and unpaid dividends due to that holder under the terms of the Merger Agreement. From and after the effective time of the merger, UWR's stock transfer books will be closed, and any certificates presented for transfer will be canceled and exchanged for the per share cash consideration in accordance with the Merger Agreement.

Lost, Stolen or Destroyed Certificates. The registered holder of a certificate representing UWR common stock which has been lost, stolen or destroyed can receive the merger consideration payable in exchange for those shares by delivering to the exchange agent an affidavit stating that the certificate has been lost, stolen or destroyed.

Representations and Warranties

UWR. In the Merger Agreement, UWR makes representations and warranties about itself and its business in favor of LAH. These representations and warranties relate to such matters as:

- the organization of UWR and its subsidiaries, their ability to conduct their respective businesses and similar corporate matters;
- UWR's capital structure;
- the authorization, execution, delivery, performance and enforceability of the Merger Agreement and the transactions contemplated by it;
- the absence of breach, violation or conflict with applicable laws, regulations, organizational documents, agreements and other existing obligations;
- regulatory approvals, licenses and permits;
- reports and financial statements filed with the SEC or appropriate state public utilities commissions or health agencies, and the accuracy of the information contained in those reports and financial statements;
- the absence of material adverse changes since June 30, 1999 and the non-occurrence of certain events;
- pending and threatened litigation;
- the accuracy of information supplied for use in this proxy statement;
- tax matters;
- retirement and other employee benefit plans and matters relating to the Employee Retirement Income Security Act of 1974, as amended;
- environmental compliance and liability;

- regulation of UWR and its subsidiaries as public utilities;
- the quality of the water supplied by UWR and its subsidiaries;
- the stockholder votes required in connection with the merger;
- the fairness opinions of Morgan Stanley;
- the taking of all action to eliminate any obligations under the Rights Agreement, dated July 12, 1989, as amended, between UWR and Chase Mellon Shareholders Services, LLC;
- the status of rights in real property held by UWR and its subsidiaries and joint ventures;
- the status of UWR's and its subsidiaries' existing franchises, easements, leases and license agreements that are necessary for UWR and its subsidiaries' respective businesses;
- the adequacy of UWR's and its subsidiaries' insurance;
- UWR's and its subsidiaries' trademarks, patents and copyrights; and
- "Year 2000" matters.

LAH. In the Merger Agreement, LAH makes representations and warranties to UWR about itself and its business. These representations and warranties relate to such matters as:

- the organization of LAH, LAH Acquisition and LAH's subsidiaries, and their ability to conduct their respective businesses and similar corporate matters;
- the authorization, execution, delivery, performance and enforceability of the Merger Agreement and the transactions contemplated by it;
- the absence of breach, violation or conflict and compliance with applicable laws, regulations, organizational documents, agreements and other existing obligations;
- regulatory approvals, licenses and permits;
- the accuracy of LAH's financial statements;
- the accuracy of information supplied for use in this proxy statement;
- LAH's ownership of UWR capital stock; and
- LAH's the ability to pay the consideration required to be paid under the Merger Agreement and to consummate the merger.

Conduct of Business Prior to the Effective Time

UWR. In the Merger Agreement, UWR has agreed that during the period from the date of the Merger Agreement until the effective time of the merger, except as otherwise permitted in the Merger Agreement or by written consent of LAH, UWR and its subsidiaries will, among other things:

- carry on their respective businesses (and those of UWR's joint ventures) in the usual, regular and ordinary course consistent with past practice;
- preserve intact its present business organization and goodwill; keep available the services of its present officers and employees as a group (subject to prudent management of workforce needs); and maintain and keep material properties in good repair;
- confer with representatives of LAH on a regular basis and notify LAH of any material changes in its business;
- use all commercially reasonable efforts to obtain third-party consents required by the Merger Agreement;

- maintain insurance coverage as is customary for companies in the water utility industry; and
- maintain all existing governmental permits pursuant to which it operates;

and will not:

- declare or pay any dividends on or make other distributions in respect of any of its capital shares, other than:
  - dividends by wholly-owned subsidiaries of UWR to UWR;
  - dividends by a less than a wholly-owned subsidiary of UWR that are consistent with past practice;
  - stated dividends on series A preference stock;
  - regular dividends on UWR common stock that, in any fiscal quarter, do not exceed 100% of the dividends for the same quarter of the previous fiscal year;
  - the additional quarterly dividends, and the special dividend, payable on UWR common stock the sum of which will equal $0.48 for each common share.
- amend its certificate of incorporation or by-laws, or take any other action which would reasonably be expected to prevent or materially impede or interfere with the merger;
- make any changes in its accounting methods other than as required by law, rule, regulation or generally accepted accounting principles;
- take any action that would, or is reasonably likely to, result in a material breach of any provision of the Merger Agreement or in UWR's representations or warranties being untrue;
- make acquisitions in excess of certain agreed amounts
- issue capital stock or other equity securities, other than certain intracompany issuances of capital stock;
- make aggregate capital expenditures in excess of certain agreed amounts;
- dispose of any assets except in the ordinary course of business consistent with past practice;
- incur or guarantee indebtedness for borrowed money in excess of certain agreed amounts;
- subject to certain exceptions, make changes to, or adopt new, employee benefit programs;
- discharge or settle any material liabilities, other than in the ordinary course of business consistent with past practice;
- modify or terminate any material contract or, except in certain circumstances, enter into any new material contract; or
- make any additional material investments or loans to any joint venture.

LAH. Pursuant to the Merger Agreement, LAH has agreed, as to itself and its subsidiaries, that, during the period from the date of the Merger Agreement until the effective time of the merger, except as otherwise permitted in the Merger Agreement or with the written consent of UWR, LAH (and each of its subsidiaries) will, among other things:

- use all commercially reasonable efforts to obtain any third-party consents required in the Merger Agreement; and
- not take any action that would or is reasonably likely to result in a material breach of any provision of the Merger Agreement or in LAH's representations and warranties being untrue.

Conditions to Consummation of the Merger

Conditions to Each Party's Obligations to Effect the Merger. Unless waived in writing, the obligations of the parties to consummate the merger are subject to satisfaction of the following conditions:

- the stockholders of UWR must have approved the Merger Agreement;
- no temporary restraining order or preliminary or permanent injunction, or other order, ruling or action taken by a United States or French federal or state court or authority shall exist which restrains, enjoins or otherwise prohibits the merger, and no law, rule, regulation or order has the effect of making completion of the merger illegal; and
- all required statutory approvals must have been obtained.

Conditions to the Obligations of LAH. The obligation of LAH to effect the merger is also subject to satisfaction of the following conditions:

- UWR must have performed, in all material respects, those agreements and covenants in the Merger Agreement required to be performed by UWR at or prior to the effective time;
- the representations and warranties of UWR contained in the Merger Agreement must be true and correct on and as of the date of the Merger Agreement and on and as of the effective time of the merger (unless the representation or warranty speaks only of a specific date other than the date of the Merger Agreement or the effective time), unless the inaccuracy could not be reasonably expected to result in a material adverse effect on the business of UWR;
- UWR must have obtained certain third-party consents;
- LAH must have received a certificate from the chief financial officer of UWR stating that the conditions to the effectiveness of the merger set forth in the Merger Agreement have been satisfied; and
- no material adverse effect on the business of UWR may have occurred or have become likely to occur.

Conditions to the Obligations of UWR. The obligation of UWR to effect the merger is subject to satisfaction of the following conditions:

- LAH must have performed, in all material respects, those agreements and covenants in the Merger Agreement required to be performed by LAH at or prior to the effective time;
- the representations and warranties of LAH contained in the Merger Agreement must be true and correct as of the date of the Merger Agreement and as of the effective time of the merger (except for a representation or warranty that speaks of a specific date other than the date of the Merger Agreement or effective time) unless the inaccuracy could not be reasonably expected to result in a material adverse effect on the business of LAH; and
- UWR must have received a certificate from the chief financial officer of LAH stating that the conditions to the effectiveness of the merger have been satisfied.

No Solicitation of Transactions

The Merger Agreement provides that between the date thereof and the effective time of the merger, UWR, its subsidiaries and its subsidiaries' directors, officers, employees, agents and representatives will immediately cease any discussions or negotiations with any parties that may be ongoing with respect to certain alternative proposals to acquire the businesses of UWR and its subsidiaries. Prior to the effective time of the merger, UWR will not, nor will it permit its subsidiaries to (a) directly or indirectly initiate, solicit or encourage any offer or proposal that constitutes or is reasonably likely to lead to an alternative proposal or (b) directly or indirectly engage in negotiations or provide confidential information or data to any person relating to an alternative proposal. UWR must notify LAH of any such inquiries, offers or proposals (including the terms and conditions of any such proposal).

The Merger Agreement does not, however, prohibit UWR, prior to obtaining the required approval of its stockholders, from (i) furnishing information to a person making an unsolicited alternative proposal which did not result from a breach of the Merger Agreement and (ii) participating in discussions with such person regarding the alternative proposal, but only to the extent that:

- the board of directors of UWR reasonably concludes in good faith (after consultation with its financial advisors) that the person or group making the alternative proposal will have adequate sources of financing to consummate the alternative proposal and that the alternative proposal is more favorable to UWR stockholders than the merger;
- the board of directors of UWR determines in good faith, based on advice of outside counsel, that it is necessary to do so to satisfy its fiduciary duties to its stockholders; and
- such person or group has entered into a confidentiality agreement containing terms no less favorable to UWR than the confidentiality agreement entered into by UWR and LAH on July 26, 1999, and the other agreements and arrangements governing UWR's relationship with LAH.

UWR will keep LAH informed on a timely and current basis on the status and details (including amendments or proposed amendments) of any request for information or alternative proposal. UWR will also immediately provide to LAH any non-public information provided to any other person in connection with an alternative proposal which was not previously provided to LAH.

The board of directors of UWR will not withdraw or modify, or propose to withdraw or modify, in any manner adverse to LAH, LAH Acquisition or both, the approval or recommendation of the board of directors of UWR of the Merger Agreement unless the board of directors of UWR has:

- determined in good faith as a result of changed circumstances, and based on the advice of outside counsel, that the board of directors' fiduciary duties require the directors to withdraw or modify their approval or recommendation; and
- provided to LAH a statement in writing in reasonable detail stating the reasons for the withdrawal or modification.

Indemnification and Insurance

The Merger Agreement provides that after the effective time of the merger, LAH and UWR will, to the fullest extent permitted by applicable law, indemnify each past and present officer and director of the parties and their subsidiaries, as well as anyone who becomes such an officer or director after the date of the Merger Agreement but prior to the effective time, against:

- liabilities and expenses (including attorneys' fees) arising out of actions or omissions made by such person at or prior to the effective time of the merger and based on the fact that such person is or was a director or officer of a party to the Merger Agreement or one of their subsidiaries; and
- all such liabilities and expenses to the extent they arise out of the Merger Agreement.

LAH is also required to maintain directors' and officers' liability insurance policies for six years following the effective time for the benefit of the persons currently covered by such policies of UWR or its subsidiaries, although LAH is not required to spend in any year more than 200% of the annual aggregate premiums currently paid by UWR for such insurance.

Workforce and Employee Benefit Matters

The Merger Agreement provides that LAH, UWR and UWR's subsidiaries will honor, without modification, all of their respective collective bargaining agreements and other contracts and agreements that apply to their current or former directors or employees, subject to any existing right to amend, modify, suspend, revoke or terminate those contracts. The parties also agreed that any workforce reductions carried out following the effective time of the merger by LAH or UWR or their subsidiaries would be done in accordance with applicable collective bargaining agreements as well as applicable laws.

Each of UWR's benefit plans (other than its stock plans) in effect at the date of the Merger Agreement will be maintained in effect with respect to the employees or former employees of UWR and any of its subsidiaries who are covered immediately prior to the effective time of the merger until LAH or UWR otherwise determine after the effective time. LAH or UWR or their subsidiaries will provide to those eligible, for a period of not less than one year following the effective time, benefits which are no less favorable in the aggregate than those provided under UWR's benefit plans (with respect to employees and former employees of UWR and its subsidiaries). Subject to certain limitations, each participant in any such benefit plan will receive credit for purposes of eligibility to participate, vesting and eligibility to receive benefits under any benefit plan of UWR, its subsidiaries or its affiliates for service credited for the corresponding purpose under such benefit plan. Nothing in the Merger Agreement limits any right contained in any such benefit plan or any applicable law to amend, modify, suspend, revoke or terminate any such plan.

With respect to any welfare benefit plan established to replace any of UWR's benefit plans which is a welfare benefit plan in which certain employees may be eligible to participate after the effective time of the merger, other than limitations, exclusions or waiting periods that are already in effect with respect to such employees and that have not been satisfied as of the effective time of the merger, such replacement plans will waive all limitations to pre-existing conditions, exclusions and waiting periods with respect to participation and coverage requirements and provide each eligible employee with credit for other co-payments and deductibles paid prior to the effective time of the merger in satisfying any applicable deductible or out-of-pocket requirements to the same calendar year under any welfare plans that such employees are eligible to participate in after the effective time. With respect to each UWR benefit plan or other plan, agreement or arrangement that provides for benefits in the form of UWR common stock or options to purchase UWR common stock, UWR and its subsidiaries and LAH and its subsidiaries will take all actions necessary to provide that upon the effective time:

- each outstanding option to purchase a share of UWR common stock under any UWR stock plan, whether or not then vested and exercisable, will be canceled in exchange for a cash payment equal to the excess of the $35.00 per share cash consideration over the exercise price of the option, net of any applicable tax withholding, and
- each outstanding restricted share of UWR common stock granted under any UWR stock plans will become fully vested as provided in the applicable stock plan and will be simultaneously converted into the right to receive the per share cash consideration of $35.00. Subject to making such payments, UWR and its subsidiaries will take all actions needed to terminate all stock plans.

Access to Information

Subject to LAH keeping non-public information confidential, UWR has agreed in the Merger Agreement to, and to cause its subsidiaries to, afford LAH and its representatives reasonable access during normal business hours to all its properties, books, contracts, commitments and records and to furnish LAH with each report, schedule and other document required by applicable federal or state securities laws or filed with any other governmental entity and to furnish LAH with all other information concerning its business, properties and personnel as LAH may from time to time reasonably request.

Modification of Existing Agreements

The terms and conditions of the Governance Agreement between LAH and UWR and the North American Rights Agreement among LAH, UWR and other parties will remain in full force and effect. However, so long as the Merger Agreement is in effect, LAH has waived the requirement under the Governance Agreement that UWR provide 30 days' prior notice before it agrees to enter into a business combination with a third party. Further, so long as the Merger Agreement is in effect, both UWR and LAH may acquire rate-regulated water and wastewater utility business in the United States in accordance with the Merger Agreement, notwithstanding any contrary provision in the North American Rights Agreement. If the Merger Agreement is terminated for reasons attributable to LAH or SLDE, UWR will have the right to acquire a 50% interest at full cost (including interest and expenses) in any rate-regulated business acquired by LAH during the time the Merger Agreement was effective. The Merger Agreement also grants to the United Water Services joint ventures a right of first refusal with respect to LAH's acquisition of non-regulated delegated services providers in the United States, Canada and Mexico, notwithstanding any contrary provision in the North American Rights Agreement. If the Merger Agreement is terminated for reasons attributable to LAH or SLDE, the United Water Services joint ventures will have the further right to buy from LAH any interests in delegated services providers actually acquired by LAH at full cost (including interest and expenses).

Termination

The Merger Agreement may be terminated at any time prior to the effective time of the merger:

- by the mutual written consent of the boards of directors of UWR and LAH;
- by either UWR or LAH if:
  - the effective time does not occur before August 20, 2000, except that this right is not available to a party whose failure to fulfill an obligation under the Merger Agreement is the cause of the effective time failing to occur. If on August 20, 2000 certain required approvals and/or consents have not been obtained, but all other conditions to closing have been fulfilled or are then capable of being met, then the August 20, 2000 deadline will be extended to February 20, 2001;
  - the merger is prohibited by any United States or French federal, state or other law, order, rule or regulation or permanently enjoined by any United States or French federal, state or other court or governmental authority of competent jurisdiction; or
  - the required approval of UWR stockholders is not obtained at a duly held special meeting, including any adjournment of such meeting.
- by LAH if:
  - UWR materially breaches the Merger Agreement in a manner that is likely to result in a material adverse effect, and such breaches are not cured within 20 days of receipt of written notice from LAH;
  - the board of directors of UWR (a) withdraws, modifies or changes, in any manner adverse to LAH, its approval or recommendation of the Merger Agreement, (b) recommends to the stockholders an alternative proposal or (c) resolves to take either such action; or
  - a tender offer or exchange offer for 20% or more of the outstanding shares of capital stock of UWR is commenced and the board of directors of UWR fails to recommend against acceptance of such tender offer or exchange offer by its stockholders (including by taking no position with respect to the acceptance of such tender offer or exchange offer by its stockholders); and
- by UWR if:
  - its board of directors exercises its fiduciary duties to stockholders in a manner consistent with certain provisions of the Merger Agreement as described in the following section, "Effect of Termination"; or

- LAH materially breaches the Merger Agreement in a manner that is likely to result in a material adverse effect, and such breach is not cured within 20 days of receipt of written notice from UWR.

Effect of Termination

If the Merger Agreement is terminated, none of UWR, LAH, LAH Acquisition or any of their respective representatives will have any liability except as specifically provided in the Merger Agreement, and, subject to certain exceptions, all rights and obligations of each party under the Merger Agreement will cease to exist.

Termination Fees and Expenses

- If UWR terminates the Merger Agreement because its board of directors determines that its fiduciary duty to its stockholders makes it necessary to accept an alternative proposal (as described above), UWR will pay to LAH a termination fee equal to $42 million plus any documented expenses incurred by LAH in connection with the Merger Agreement up to $3 million.
- LAH may terminate the Merger Agreement if (i) UWR's board of directors withdraws or changes its approval or recommendation of the Agreement in a manner adverse to LAH or resolves to do so, (ii) UWR's board of directors recommends to stockholders an alternative proposal to UWR stockholders or resolves to do so, or (iii) a tender offer or exchange offer for 20% or more of the outstanding shares of capital stock of UWR is commenced and the board of directors of UWR fails to recommend to its stockholders against the tender offer or exchange offer. If LAH terminates the Merger Agreement for any of those reasons, and UWR enters into a definitive acquisition, merger or similar agreement to effect an alternative proposal within two years of the date of termination, then UWR must pay to LAH its documented expenses up to $3 million and the $42 million termination fee.
- IF UWR or LAH terminates the Merger Agreement because the UWR stockholders do not approve the Merger Agreement, and at the time of such failure, a third party has made a public announcement or communicated to UWR or its stockholders concerning an alternative proposal that has not been rejected by UWR and withdrawn or terminated by the party making it, and if UWR enters into a definitive agreement to effect an alternative proposal within two years of the date of the termination, then UWR has agreed to pay LAH its documented expenses up to $3 million plus the $42 million termination fee.

Amendment and Waiver

Amendment. UWR and LAH may amend the Merger Agreement by action taken by their boards of directors at any time before the effective time. After the stockholders of UWR have approved the merger, however, no amendment may be made that:

- alters or changes the treatment of shares of UWR capital stock under the Merger Agreement; or
- alters or changes the terms of the Merger Agreement that would, alone or in the aggregate, materially alter the rights of holders of UWR capital stock, except for alterations or changes that could otherwise be adopted by the board of directors without the further approval of UWR stockholders.

Waiver. At any time prior to the effective time, the parties may:

- extend the time for performance of acts or obligations of the other parties;
- waive inaccuracies in the representations and warranties of the other parties; and
- waive compliance with agreements or conditions contained in the Merger Agreement, to the extent permitted by applicable law.

Assignment

LAH and LAH Acquisition may assign any or all of their rights and obligations under the Merger Agreement to any wholly-owned subsidiary of LAH, but the assigning party will remain responsible for the performance of the assigned obligations if the assignee does not perform them.

THE COMPANIES

UWR
200 Old Hook Road
Harrington Park, New Jersey 07640

UWR is a holding company primarily engaged in water-related businesses. As the second-largest investor-owned water services company in the United States, UWR provides water and wastewater services through its regulated utilities and nonregulated contract operations (some of which are owned jointly with LAH) to over 7.5 million people in more than 400 communities in 19 states. UWR also has investments in water services in Canada and Mexico in which LAH is a majority owner. In addition, UWR owns and manages real estate investments through a wholly-owned subsidiary. UWR has been listed on the New York Stock Exchange since 1889 and has paid cash dividends on its common stock continuously since 1886.

1. *United Water New Jersey Inc.*

United Water New Jersey Inc. is a wholly owned subsidiary that supplies water service to over 179,000 customers in 60 municipalities in the northeastern part of New Jersey, serving most of Bergen County and the northern part of Hudson County. The total population served is about 750,000 persons.

2. *United Waterworks Inc.*

United Waterworks Inc. is a wholly owned subsidiary that provides water and wastewater services to a total of approximately 360,000 customers in 13 states through its regulated water and wastewater utility subsidiaries. The utility subsidiaries and United Waterworks serve a total population of about 1,000,000.

3. *United Properties Group, Incorporated*

United Properties Group, Incorporated is a wholly owned subsidiary that, with its subsidiaries, constitute a non-regulated business engaged in real estate investment and development activities, including commercial office and retail properties, residential and commercial land development and sales, golf course operations and consulting services. United Properties owns and manages a portfolio of real estate located in New Jersey, New York, Delaware, Idaho and Florida. It also provides consulting and advisory services in support of the real estate assets of the other United Water companies.

4. *United Water Mid-Atlantic Inc.*

A wholly-owned subsidiary of United Water Resources, United Water Mid-Atlantic, through its subsidiaries, owns and operates several small water and wastewater utility systems that provide water supply, wastewater connection and wastewater transmission services to approximately 6,300 customers primarily in Plainsboro, Vernon Township and Mt. Arlington, New Jersey.

5. *United Water Operations Inc.*

United Water Operations Inc. is a wholly-owned subsidiary that serves as a holding company for United Water Resources Inc. operating ventures, including those in Jersey City, Manalapan, and Hoboken, New Jersey.

6. *United Water Management and Services Inc.*

United Water Management and Services Inc. is a wholly-owned subsidiary that provides management services to various United Water entities.

7. *United Water USA Inc.*

United Water USA Inc. is a wholly-owned, special purpose subsidiary that owns a 50% stake in United Water Services LLC.

8. United Water Canada Inc.

United Water Canada Inc. is wholly-owned, special purpose subsidiary that owns a 33⅓% stake in United Water Services Canada L.P.

9. United Water Mexico Inc.

United Water Mexico Inc. is wholly-owned, special purpose subsidiary that owns a 20.5% stake in United Water Services Mexico L.L.C.

10. United Water UK Limited

United Water UK Limited is a wholly-owned subsidiary that is an equal partner with Lyonnaise Europe plc in the Northumbrian Partnership (each with a 50% interest). The Northumbrian Partnership owns a 20% interest in Northumbrian Water Group plc, a major water and wastewater company in the United Kingdom that is a majority-owned affiliate of SLDE.

SLDE
1, rue d'Astorg
75008 Paris, France

SLDE, a société anonyme organized and existing under the laws of the Republic of France, operates infrastructure services in more than 120 countries, providing electricity and natural gas, waste services, communications services and water services, and maintains interests in construction and capital investments. SLDE was formed from the 1997 merger of Compagnie de Suez (builder of the Suez Canal) and Lyonnaise des Eaux. SLDE's registered office is located at 72 Avenue de la Liberte, 92022 Nanterre Cedex, France and the principal address of SLDE's water division is 18 Square Edouard VII, 75316 Paris Cedex 09, France.

LAH
2000 First State Boulevard
Wilmington, Delaware 19804-0507

LAH is a Delaware corporation with its principal business as a holding company of (i) its ownership interest in UWR, (ii) 50% of United Water Services LLC, a Delaware limited liability company which provides services in the water and wastewater industries to municipalities in the United States, (iii) majority interests in United Water Services Canada L.P., an Ontario, Canada limited partnership, and United Water Services Mexico LLC, a Delaware limited liability company, which provide services in the water and wastewater industries to municipalities in Canada and Mexico, respectively, and (iv) a 49% interest in Technologia y Servicios De Agua, S.A., a Mexican company which provides certain water services to the city of Mexico City, Mexico. All of the issued and outstanding shares of capital stock of LAH are owned beneficially and of record by SLDE. The principal business mailing address of LAH is c/o United Water Services LLC, 200 Old Hook Road, Harrington Park, New Jersey 07640, and the address of its principal office is 2000 First State Boulevard, Wilmington, Delaware 19804-0508.

LAH Acquisition
c/o United Water Services LLC
200 Old Hook Road
Harrington Park, New Jersey 07640

LAH Acquisition is a wholly-owned special purpose subsidiary of LAH, formed under the laws of the State of New Jersey solely for the purpose of the merger. LAH Acquisition has not conducted any business other than in connection with the Merger Agreement. All of the issued and outstanding shares of capital stock of LAH Acquisition are owned beneficially and of record by LAH. The principal business mailing address of LAH Acquisition is c/o United Water Services LLC, 200 Old Hook Road, Harrington Park, New Jersey 07640, and the address of its principal office is 1013 Centre Road, Wilmington, Delaware 19805-1297.

Recent Transactions Between UWR, LAH and SLDE

Purchases of UWR Stock by LAH and SLDE. Neither SLDE nor LAH Acquisition has made any purchases of UWR common stock and none of SLDE, LAH nor LAH Acquisition has made any purchases of Series A Preference Stock since January 1, 1997, the commencement of UWR's second full fiscal year preceding the date of this proxy statement. All purchases of UWR common stock made by LAH during such period were made by reinvesting cash dividends paid by UWR on the UWR common stock pursuant to UWR's Dividend Reinvestment and Stock Purchase Plan (the "DRIP Program"), as follows:

Date	Dollar Amount Reinvested	No. of Shares Acquired	Price Per Share
March 1, 1997	$2,188,606.86	123,388.6827	$17.7375
June 2, 1997	$2,285,181.16	127,574.6635	$17.9125
September 2, 1997	$2,314,523.33	128,853.0733	$17.9625
December 1, 1997	$2,344,159.54	135,158.3586	$17.3438
March 2, 1998	$2,375,245.96	124,603.0668	$19.0625
June 2, 1998	$2,466,804.83	148,379.2379	$16.6250
September 1, 1998	$2,500,932.06	140,649.5622	$17.7813
December 1, 1998	$2,643,424.13	134,056.0343	$19.7188
March 1, 1999	$2,675,597.58	131,357.6440	$20.3688
June 1, 1999	$2,774,001.09	128,686.3279	$21.5563

During this period, LAH also acquired shares of UWR common stock through conversion of shares of UWR's series A preference stock, as follows; (i) on April 22, 1997, LAH converted 355,802 shares of series A preference stock into 296,500 shares of UWR common stock at the conversion ratio of 0.83333 shares of UWR common stock for each share of series A preference stock; (ii) on April 22, 1998, LAH converted 328,177 shares of series A preference stock into 273,479 shares of UWR common stock at the conversion ratio of 0.83333 shares of UWR common stock for each share of series A preference stock; and (iii) on April 22, 1999, LAH converted 334,390 shares of series A preference stock into 278,657 shares of UWR common stock at the conversion ratio of 0.83333 shares of UWR common stock for each share of series A preference stock. No funds were paid by LAH to effect the conversion of any such shares of series A preference stock.

Certain Other Transactions. Since January 1, 1997 (the commencement of UWR's second full fiscal year preceding the date of this proxy statement), the following transactions have been entered into between SLDE, LAH, and their subsidiaries and UWR.

On July 28, 1997, UWR, LAH, SLDE, Montgomery Watson Inc., and certain of their existing and newly-formed subsidiaries completed a reorganization of the parties' North American delegated services (non-regulated) water and wastewater businesses. In the reorganization, (i) UWR and LAH converted an existing partnership into United Water Services LLC, a Delaware limited liability company in which each of LAH and UWR owns 50% of the voting interests and Montgomery Watson owns a non-voting interest (which is convertible into a 10% voting interest); (ii) LAH, UWR and Montgomery Watson contributed cash and certain existing Canadian operations to United Water Services Canada L.P., a newly-formed Ontario, Canada limited partnership, in exchange for ownership interests of 60%, 30% and 10%, respectively, (iii) LAH, UWR and Montgomery Watson contributed cash and certain existing Mexican operations to United Water Services Mexico LLC, a newly-formed Delaware limited liability company, in exchange for ownership interests of 70%, 20% and 10% respectively, (iv) United Water Services LLC acquired Montgomery Watson's 50% stake in

United Water Services Inc. (formerly known as JMM Operational Services Inc.), as a result of which United Water Services Inc. became a wholly-owned subsidiary of United Water Services LLC (prior to the restructuring, United Water Services LLC owned a 50% interest in United Water Services Inc., and Montgomery Watson owned the remaining 50% interest); and (v) the parties entered into related agreements for, among other things, certain exclusive dealings with the reorganized entities, the provision of technical and advisory services to the reorganized entities and the use of UWR's trademarks by the reorganized entities.

The agreed value of the parties' contributions to each of the reorganized entities was as follows:

	United Water Services LLC	United Water Services Canada L.P.	United Water Services Mexico LLC
SLDE/LAH	$30,667,500	$1,727,400	$2,389,800
UWR	$30,667,500	$ 863,700	$ 682,800
Montgomery Watson	$ 6,815,000	$ 287,900	$ 342,400

In December 1998, Montgomery Watson sold its interests in United Water Services Canada L.P. and United Water Services Mexico LLC to LAH and UWR. As a result United Water Services Canada L.P. is now owned 66.7% by LAH and 33.3% by UWR while United Water Services Mexico LLC is now owned 79.5% by LAH and 20.5% by UWR.

Certain of the municipalities with which the reorganized entities or their subsidiaries have contracted to provide water and/or wastewater treatment services required, as a condition to the awarding of the contract, that the entity's performance be guaranteed by one or more of its corporate parents. Each of UWR, LAH and Montgomery Watson has agreed to share liability for payments made and costs incurred under these performance guarantees in proportion to its ownership of the entity whose obligations are guaranteed.

In 1997, United Water Services LLC bought from UWR a 100% ownership interest in United Metering Inc., a company that provides water meter installation and maintenance services.

SELECTED HISTORICAL FINANCIAL INFORMATION

The following table sets forth selected consolidated historical financial data of UWR and has been derived from, and should be read in conjunction with, the audited consolidated financial statements of UWR for each of the five years ended December 31, 1998 and the unaudited interim consolidated financial statements of UWR for the nine months ended September 30, 1999 and 1998, including the respective notes thereto. In the opinion of management, all adjustments, consisting of normal recurring accruals considered necessary for a fair presentation have been included in the unaudited interim data. Interim results for the nine months ended September 30, 1999 are not necessarily indicative of results which may be expected for future periods, including the year ended December 31, 1999.

	Nine months ended September 30,		**Year ended December 31,**				
	1999	**1998**	**1998**	**1997**	**1996**	**1995**	**1994**
			(In thousands, except per share data)				
Consolidated Income Statement Data:							
Operating revenues from continuing operations		$ 270,409	$ 356,210	$ 351,409	$ 332,045	$ 319,536	$ 284,767
Operating income		75,473	97,600	95,644	95,699	82,183	83,847
Income from continuing operations		36,764	47,987	33,676	43,020	24,760	31,611
Preferred and preference stock dividends		3,088	4,058	4,345	4,613	4,795	3,454
Net income from continuing operations	—	33,676	43,929	29,331	38,407	19,965	28,157
Loss from discontinued operations	—	—	—	—	(4,397)	(2,622)	(270)
Net income	$—	$ 33,676	$ 43,929	$ 29,331	$ 34,010	$ 17,343	$ 27,887
Basic earnings/(loss) per share							
From continuing operations		$ 0.91	$ 1.19	$ 0.83	$ 1.14	$ 0.62	$ 1.02
From discontinued operations	—	—	—	—	(0.05)	(0.08)	(0.01)
From disposal of discontinued operations	—	—	—	—	(0.08)	—	—
Basic earnings/(loss) per share	$—	$ 0.91	$ 1.19	$ 0.83	$ 1.01	$ 0.54	$ 1.01
Weighted average common shares outstanding		36,848	37,028	35,492	33,707	31,995	27,524
Diluted earnings/(loss) per share							
From continuing operations		$ 0.90	$ 1.17	$ 0.83	$ 1.12	$ 0.62	$ 1.02
From discontinued operations	—	—	—	—	(0.04)	(0.08)	(0.01)
From disposal of discontinued operations	—	—	—	—	(0.08)	—	—
Diluted earnings/(loss) per share	$—	$ 0.90	$ 1.17	$ 0.83	$ 1.00	$ 0.54	$ 1.01
Weighted average common shares outstanding		39,023	39,192	37,838	36,218	31,995	27,524
Dividends declared per common share		0.69	0.93	0.92	0.92	0.92	0.92
Balance Sheet Data: (at end of period)							
Total assets		1,719,857	1,769,122	1,658,342	1,582,097	1,516,708	1,457,427
Long-term obligations		618,714	652,969	622,737	558,093	558,658	505,204
Stockholders' equity		537,072	545,311	514,180	493,751	465,393	457,668
Book value per common share		11.95	12.05	11.53	11.33	10.90	11.20

PRICE OF UWR COMMON STOCK AND DIVIDENDS

UWR's common stock is traded on the New York Stock Exchange under the symbol "UWR." The high and low sales prices per quarter for UWR's common stock through the third quarter of 1999, and for the years of 1998, 1997 and 1996 and the dividends paid on the common stock in each quarter, were as follows:

QUARTER	STOCK PRICE HIGH	STOCK PRICE LOW	DIVIDEND
1999			
Fourth through October 4, 1999	$33.000	$32.625	$
Third	33.750	20.750	.24
Second	23.688	20.000	.24
First	24.062	18.438	.24
1998			
Fourth	$25.000	$16.500	$.24
Third	19.250	16.375	.23
Second	18.438	15.750	.23
First	19.875	17.500	.23
1997			
Fourth	$19.750	$16.000	$.23
Third	19.813	17.000	.23
Second	19.375	16.375	.23
First	18.500	15.000	.23
1996			
Fourth	$16.625	$14.625	$.23
Third	17.500	12.750	.23
Second	13.500	12.000	.23
First	13.240	12.000	.23

On August 17, 1999, the last trading day before public announcement that UWR was engaged in merger negotiations, the last sale price of UWR common stock on the New York Stock Exchange Composite Transactions Tape was $24.53 per share.

On October 4, 1999, the most recent practicable date prior to the printing of this proxy statement, the last sale price of common stock as reported on the New York Stock Exchange Composite Transactions Tape was $33.000 per share.

OWNERSHIP OF SECURITIES BY DIRECTORS, EXECUTIVE OFFICERS AND CERTAIN BENEFICIAL OWNERS

The following information pertains to the common stock of UWR beneficially owned, directly or indirectly, by each director and named executive officers individually and by all directors and executive officers of UWR and its subsidiaries as a group as of September 30, 1999.

Name of Beneficial Owner	Number of Shares (a)(d)
Edward E. Barr	31,276(b)(e)
Frank J. Borelli	9,622
Thierry Bourbié	4,551
Charles Chaumin	3,181
Lawrence R. Codey	5,786
Donald L. Correll	187,758(c)
Peter Del Col	12,862
Frank J. DeMicco	30,474(c)
Robert L. Duncan, Jr	5,361
Michael C. J. Fallon	28,871(c)
Jon F. Hanson	37,887(b)(e)
Douglas W. Hawes	15,741
George F. Keane	5,425
Richard B. McGlynn	47,892(c)
Dennis M. Newnham	6,547
Joseph Simunovich	76,271(c)
Marcia L. Worthing	10,243(e)
Directors and Executive Officers as a Group (24 persons)	744,445(b)(c)

(a) None of the directors or executive officers of UWR owns equity securities of UWR or any of its subsidiaries other than common stock. As of September 30, 1999, each director or executive officer beneficially owned less than 0.5% of the outstanding common stock of UWR and all of the directors and executive officers as a group beneficially owned less than 2.0% of such stock. Fractional shares have been rounded to the nearest whole share.

(b) Includes, in compliance with applicable regulations and interpretations, shares of common stock held by the spouse or other relatives who share the home, in custody for children or grandchildren of the persons indicated or indirectly through a trust or similar arrangement in the following amounts: J. Hanson (16,845); E. Barr (10,000); and all directors and executive officers as a group (27,098). Such persons disclaim any beneficial ownership of such shares.

(c) Includes shares of common stock which may be acquired pursuant to options awarded under UWR's Management Incentive Plan in the following amounts: D. Correll (124,040); F. DeMicco (28,700); M. Fallon (24,710); R. McGlynn (45,590); J. Simunovich (70,960); and all directors and executive officers as a group (498,890).

(d) Includes shares of restricted common stock granted pursuant to the Directors' Restricted Stock Plans totalling 63,478 shares.

(e) Includes non-voting common stock equivalent units acquired in accordance with the non-employee Directors' Deferred Compensation Unit Plan in the following amounts: E. Barr (4,872); J. Hanson (14,993); and M. Worthing (3,311).

Non-Employee Directors' Deferred Compensation Unit Plan

On January 1, 1996 the UWR board of directors replaced its existing directors' deferred compensation plan with the United Water Resources and Subsidiaries Non-Employee Directors' Deferred Compensation Unit Plan. The purpose of the plan is to further UWR's long-term objectives by linking the personal interests of participating directors to those of UWR stockholders. In addition to converting all amounts previously deferred by directors under the predecessor deferred compensation plan, the new plan allows each director to defer the receipt of all or a portion of his or her annual retainer and meeting fees in the form of non-voting common stock equivalent units, equal in value to shares of UWR common stock. The value of each unit increases and decreases in accordance with the fluctuations in value of UWR's common stock. Additionally, dividend equivalent units accrue on the units as cash or stock dividends are distributed with respect to UWR common stock. Thus, the ultimate value of the directors' accounts depends on the performance of UWR common stock and the dividends declared with respect to such stock. All amounts in a director's account are distributed in the form of cash to the director, or his or her beneficiary if the director is deceased, on the date previously specified in the deferral election form completed by the director.

FIVE PERCENT OWNER OF UWR COMMON STOCK

The following corporation is known to UWR to be the beneficial owner of more than 5% of a class of UWR's voting securities. To the knowledge of UWR, no other person is the holder of more than 5% of any class of UWR's voting securities as of September 30, 1999.

Title of Class	Name and Address of Beneficial Owner	Amount and Nature of Beneficial Ownership	Percent of Class
Common Stock	Lyonnaise American Holding, Inc. 2000 First State Boulevard Wilmington, Delaware 19804-0507	11,687,024 shares	30.1%

LAH, its parent company SLDE, and certain of their respective affiliates are subject to the terms of a Governance Agreement, dated April 22, 1994, which, among other things, prohibits, subject to certain exceptions, such parties from acquiring additional UWR securities, commencing unsolicited tender or exchange offers to acquire UWR's securities, making offers to acquire UWR's assets or soliciting proxies against UWR's management and which requires their common stock to be voted in accordance with the votes of the holders of 75% of the common stock if any proposal obtains that vote. SLDE, LAH and UWR, pursuant to the Merger Agreement, have modified the Governance Agreement in order to allow for the acquisition of UWR common stock and series A preference stock contemplated in the merger.

MERGER RELATED FINANCING

It is estimated that the total amount of funds required by LAH to consummate the acquisition of the capital stock of UWR not already owned by it is approximately $1 billion. In the Merger Agreement, SLDE has agreed to cause LAH and LAH Acquisition to have sufficient funds to consummate the merger at the effective time and to meet their other financial obligations under the Merger Agreement.

SLDE and LAH expect to fund the cost of the acquisition using currently available cash resources and other existing and new capital resources, which may include syndicated borrowing from banks, public issuance of debt and equity securities and the private placement of debt securities. As of December 31, 1998, SLDE had cash and cash equivalents of approximately 2.8 billion euros (approximately $3.3 billion), debt of approximately 21.5 billion euros (approximately $25.4 billion) and stockholders equity of approximately 8.9 billion euros (approximately $10.5 billion).

It is estimated that the expenses incurred by the parties with respect to the merger will be as follows:

Item	$
SEC Filing Fees	
Legal fees	
Accounting fees	
Appraisal fees	
Solicitation expenses	
Printing costs	
Other Miscellaneous expenses	

In accordance with the merger agreement, all costs and expenses in connection with the merger will be paid by the party incurring such expenses.

OTHER MATTERS

UWR presently does not intend to bring before its special meeting any matters other than those specified and does not have any knowledge of any other matters which may be brought up by other persons. However, if any other matters not now known properly come before the UWR special meeting or any adjournments thereof, the persons named in the enclosed form of proxy, including any substitutes, will vote such proxies in accordance with their judgment on such matters.

ANNEX A

AGREEMENT AND PLAN OF MERGER

by and among

UNITED WATER RESOURCES INC.,

LYONNAISE AMERICAN HOLDING, INC.,

LAH ACQUISITION CO.

and

SUEZ LYONNAISE DES EAUX,

dated as of August 20, 1999

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PROVISIONS RELATING TO SLDE

This AGREEMENT AND PLAN OF MERGER dated as of August 20, 1999 (this "*Agreement*") is made and entered into by and among United Water Resources Inc., a New Jersey corporation (the "*Company*"), Lyonnaise American Holding, Inc., a Delaware corporation ("Parent"), LAH Acquisition Co., a New Jersey corporation and a wholly owned subsidiary of Parent ("*Merger Sub*"), and, solely with respect to the provisions of Article XI, Suez Lyonnaise des Eaux, a French société anonyme ("SLDE");

WHEREAS, the boards of directors of the Company, Parent and Merger Sub have approved and deemed it advisable and in the best interests of their respective stockholders to consummate the transactions contemplated herein under which the business of the Company and Parent would be combined by means of the merger of Merger Sub with and into the Company, as a result of which the Company will become a wholly owned subsidiary of Parent (the "*Merger*");

WHEREAS, the Company, Parent and Merger Sub desire to make certain representations, warranties and agreements in connection with the Merger and to prescribe various conditions to the Merger; and

WHEREAS, SLDE has agreed to the obligations contained in Article XI of this Agreement.

NOW THEREFORE, in consideration of the foregoing and the respective representations, warranties, covenants and agreements contained herein, the parties hereto, intending to be legally bound hereby, agree as follows:

ARTICLE I

THE MERGER

SECTION 1.1 ***The Merger.*** Upon the terms and subject to the conditions of this Agreement, at the Effective Time of the Merger (as defined in *Section 1.2*) Merger Sub shall be merged with and into the Company in accordance with the Business Corporation Act of the State of New Jersey (the "*NJBCA*"). Following the Merger, the separate corporate existence of Merger Sub shall cease and the Company shall be the surviving corporation (the "*Surviving Corporation*") and shall continue its corporate existence under the laws of the State of New Jersey.

SECTION 1.2 ***Effective Time of the Merger.*** A certificate of merger (the "*Certificate of Merger*") shall be duly prepared and executed by the Surviving Corporation and thereafter delivered to the office of the Secretary of State of the State of New Jersey (the "*Secretary of State*") for filing, as provided in Section 14A:10-4.1 of the NJBCA, on the Closing Date. The Merger shall become effective at such time as the Certificate of Merger is duly filed with the Secretary of State or at such subsequent time as Parent and the Company shall agree and specify in the Certificate of Merger (the date and time the Merger becomes effective being the "*Effective Time*").

SECTION 1.3 ***Effects of the Merger.*** Subject to the foregoing, the effects of the Merger shall be as provided in the applicable provisions of the NJBCA.

SECTION 1.4 ***Certificate of Incorporation and By-laws of the Surviving Corporation.*** At the Effective Time, (i) the certificate of incorporation of Merger Sub, as in effect immediately prior to the Effective Time, shall become the certificate of incorporation of the Surviving Corporation until thereafter amended as provided by law and such certificate of incorporation and (ii) the by-laws of Merger Sub as in effect immediately prior to the Effective Time shall be the by-laws of the Surviving Corporation until thereafter amended as provided by law, the certificate of incorporation of the Surviving Corporation and such by-laws.

SECTION 1.5 ***Directors and Officers of the Surviving Corporation.*** The directors of Merger Sub and the officers of the Company immediately prior to the Effective Time shall, from and after the Effective Time, be the directors and officers, respectively, of the Surviving Corporation until their successors shall have been duly elected or appointed and qualified or until their earlier death, resignation or removal in accordance with the Surviving Corporation's certificate of incorporation and by-laws.

SECTION 1.6 *Further Actions.* At and after the Effective Time, the officers and directors of the Surviving Corporation will be authorized to execute and deliver, in the name and on behalf of the Company or Merger Sub, any deeds, bills of sale, assignments or assurances and to take and do, in the name and on behalf of the Company or Merger Sub, any other actions and things to vest, perfect or confirm of record or otherwise in the Surviving Corporation any and all right, title and interest in, to and under any of the rights, properties or assets acquired or to be acquired by the Surviving Corporation as a result of, or in connection with, the Merger.

ARTICLE II

TREATMENT OF SHARES

SECTION 2.1 *Effect of the Merger on Capital Stock.* At the Effective Time by virtue of the Merger and without any action on the part of any holder of any capital stock of the Company or Merger Sub:

(a) *Conversion of Merger Sub Stock.* Each issued and outstanding share of common stock, par value $1.00 per share, of Merger Sub shall be converted into one fully paid and non-assessable share of common stock, no par value, of the Surviving Corporation (the "*Surviving Corporation Common Stock*").

(b) *Cancellation of Certain Company Stock.* Each share of common stock, no par value, of the Company (the "*Company Common Stock*"), together with the associated Right (as defined in *Section 4.16*) to purchase Company Preferred Stock pursuant to the Company Rights Agreement (as defined in *Section 4.16*), and each share of 5% Series A Cumulative Convertible Preference Stock, no par value, of the Company ("*Series A Preference Stock*") that is owned by the Company as treasury stock and all shares of Company Common Stock (and associated Rights) and Series A Preference Stock that are owned, directly or indirectly, by the Company or Parent or any of their respective wholly-owned subsidiaries shall be canceled and retired and shall cease to exist, and no consideration shall be delivered in exchange therefor.

(c) *Conversion of Company Common Stock.* Each issued and outstanding share of Company Common Stock, together with the associated Rights, other than shares and Rights canceled pursuant to *Section 2.1(b)* of this Agreement, shall be converted into the right to receive $35.00 per share, without interest (the "*Per Share Cash Consideration*"). Each share of Company Common Stock and each associated Right converted in accordance with this paragraph 2.1(c) shall no longer be outstanding and shall automatically be canceled and retired and shall cease to exist. Each holder of a certificate formerly representing any such shares of Company Common Stock shall cease to have any rights with respect thereto, except the right to receive the Per Share Cash Consideration to be issued in consideration therefor upon surrender of such certificate in accordance with *Section 2.2* and any dividends declared and unpaid as of the Effective Time.

(d) *Conversion of Series A Preference Stock.* Each issued and outstanding share of Series A Preference Stock, other than shares canceled pursuant to *Section 2.1(b)* of this Agreement, shall be converted automatically into the right to receive an amount in cash equal to the product of the Per Share Cash Consideration multiplied by the number of shares of Company Common Stock into which such share of Series A Preference Stock is convertible immediately prior to the Effective Time. Each share of Series A Preference Stock converted in accordance with this paragraph 2.1(d) shall no longer be outstanding and shall automatically be canceled and retired and shall cease to exist. Each holder of a certificate formerly representing any such shares of Series A Preference Stock shall cease to have any rights with respect thereto, except the right to receive the Per Share Cash Consideration to be issued in consideration therefor upon surrender of such certificate in accordance with *Section 2.2* and any dividends declared and unpaid as of the Effective Time.

SECTION 2.2 ***Exchange of Certificates.*** (a) *Exchange Agent.* At the Effective Time, Parent shall deposit with a bank or trust company mutually agreeable to Parent and the Company (the "*Exchange Agent*"), pursuant to an agreement with the Exchange Agent in form and substance reasonably acceptable to Parent and the Company, an amount in cash equal to the sum of (i) the Per Share Cash Consideration multiplied by the number of shares of Company Common Stock to be converted into the right to receive the Per Share Cash Consideration as determined in *Section 2.1(c)* plus (ii) the Per Share Cash Consideration multiplied by the number of shares of Company Common Stock into which the Series A Preference Stock is convertible as determined in *Section 2.1(d)* plus (iii) the amount of any dividends which were declared in respect of Company Common Stock and the Series A Preference Stock with a record date prior to the Effective Time and which remain unpaid at the Effective Time (the "*Unpaid Company Dividends*"). Any cash deposited with the Exchange Agent shall hereinafter be referred to as the "Exchange Fund."

(b) *Payment of Cash Consideration.* Promptly after the Effective Time, Parent and the Surviving Corporation shall cause the Exchange Agent to mail to each holder of record as of the Effective Time of a certificate or certificates which immediately prior to the Effective Time represented outstanding shares of Company Common Stock or Series A Preference Stock (the "*Certificates*") that were converted into the right to receive the Per Share Cash Consideration pursuant to *Section 2.1*: (i) a letter of transmittal (which shall specify that delivery shall be effected, and risk of loss and title to the Certificates shall pass, only upon actual delivery of the Certificates to the Exchange Agent and shall be in such form and have such other provisions as Parent and the Surviving Corporation may reasonably specify) and (ii) instructions for effecting the surrender of the Certificates in exchange for the Per Share Cash Consideration. Upon surrender of a Certificate to the Exchange Agent for cancellation, together with a duly executed letter of transmittal and such other documents as the Exchange Agent may require, the holder of such Certificate shall be entitled to receive in exchange therefor a bank check for an amount equal to the sum of (x) the Per Share Cash Consideration multiplied by (A) if such Certificate evidenced one or more shares of Company Common Stock, the number of shares of Company Common Stock evidenced thereby or (B) if such Certificate evidenced one or more shares of Series A Preference Stock, the number of shares of Company Common Stock into which the shares of Series A Preference Stock evidenced thereby were convertible immediately prior to the Effective Time plus, in either case, (y) any Unpaid Company Dividends payable in respect of such shares (such sum being referred to as the "Cash Consideration"). In no event shall the holder of any such surrendered Certificates be entitled to receive interest on any cash to be received in the Merger. If such check is to be issued in the name of a person other than the person in whose name the Certificates surrendered for exchange therefor are registered, it shall be a condition of the exchange that the person requesting such exchange shall pay to the Exchange Agent any transfer or other taxes required by reason of issuance of such check to a person other than the registered holder of the Certificates surrendered, or shall establish to the satisfaction of the Exchange Agent that such tax has been paid or is not applicable. Until surrendered as contemplated by this *Section 2.2*, each Certificate shall be deemed at any time after the Effective Time to represent only the right to receive upon such surrender the Cash Consideration as contemplated by this *Section 2.2*. If for any reason (including losses) the Exchange Agent is unable to pay the cash amounts to which holders of the Certificates shall be entitled, Parent shall in any event remain liable, and shall make available to the Surviving Corporation additional funds, for the payment thereof.

(c) *Closing of Transfer Books.* From and after the Effective Time the stock transfer books of the Company shall be closed and no transfer of any capital stock of the Company shall thereafter be made. If, after the Effective Time, Certificates are presented to the Surviving Corporation, they shall be canceled and exchanged for the Cash Consideration as provided in *Section 2.1* and in this *Section 2.2*.

(d) *Termination of Exchange Agent.* All funds held by the Exchange Agent in the Exchange Fund for payment to the holders of Certificates unclaimed at the end of one year from the Effective Time shall be returned to the Surviving Corporation, after which time any holder of Certificates who has not theretofore complied with this Article II shall thereafter look as a general creditor only to Parent for payment of the Cash Consideration to which such holder may be due, subject to applicable law.

(e) *Investment of the Exchange Fund.* The Exchange Agent shall invest any cash included in the Exchange Fund only in one or more of the following investments as directed by the Surviving Corporation from time to time: (i) obligations of the United States government maturing not more than 90 days after the date of purchase; (ii) certificates of deposit maturing not more than 90 days after the date of purchase issued by a bank organized under the laws of the United States or any state thereof having a combined capital and surplus of at least $500,000,000; (iii) a money market fund having assets of at least $3,000,000,000; or (iv) tax-exempt or corporate debt obligations maturing not more than 90 days after the date of purchase given the highest investment grade rating by Standard & Poor's and Moody's Investor Service. Any interest and other income resulting from such investments shall promptly be paid to the Surviving Corporation.

(f) *Lost Certificates.* If any Certificate shall have been lost, stolen or destroyed, upon the making of an affidavit of that fact by the stockholder claiming such Certificate to be lost, stolen or destroyed and, if required by the Surviving Corporation, the posting by such stockholder of a bond in such reasonable amount as the Surviving Corporation may direct as indemnity against any claim that may be made against it with respect to such Certificate, the Exchange Agent will deliver in exchange for such lost, stolen or destroyed Certificate the applicable Cash Consideration with respect to the shares of Company Common Stock or Series A Preference Stock formerly represented thereby.

(g) *Escheat.* The Surviving Corporation shall not be liable to any person for funds delivered to a public official pursuant to any applicable abandoned property, escheat or similar law.

ARTICLE III

THE CLOSING

SECTION 3.1 ***Closing.*** The closing of the Merger (the "*Closing*") shall take place at the offices of Piper & Marbury L.L.P., 1251 Avenue of the Americas, New York, New York, at 10:00 A.M., New York time, on the second business day immediately following the date on which the last of the conditions set forth in *Article VIII* hereof is fulfilled or waived (other than conditions that by their nature are required to be performed on the Closing Date, but subject to satisfaction of such conditions), or at such other time and date and place as the Company and Parent shall mutually agree (the "*Closing Date*").

ARTICLE IV

REPRESENTATIONS AND WARRANTIES OF THE COMPANY

The Company represents and warrants to Parent and Merger Sub as follows:

SECTION 4.1 ***Organization and Qualification.*** Except as set forth in Section 4.1 of the Company Disclosure Schedule (as defined in *Section 7.6(ii)*), the Company and each subsidiary (as defined below) of the Company is a corporation duly organized, validly existing and in good standing under the laws of its jurisdiction of incorporation or organization, has all requisite corporate power and authority, and has been duly authorized by all necessary approvals and orders, to own, lease and operate its assets and properties to the extent owned, leased and operated and to carry on its business as it is now being conducted and is duly qualified and in good standing to do business in each jurisdiction in which the nature of its business or the ownership or leasing of its assets and properties makes such qualification necessary, other than in such jurisdictions where the failure to be so qualified and in good standing will not, when taken together with all other such failures, have a Company Material Adverse Effect. As used in this Agreement, "Company Material Adverse Effect" means any change, effect, condition or circumstance that is reasonably likely to be materially adverse to the business, properties, condition (financial or otherwise) or results of operations of the Company and its subsidiaries, taken as a whole, or the consummation of the transactions contemplated by this Agreement, excluding (i) any occurrence affecting the United States water supply and waste water services industry as a whole, (ii) any adverse effect to the extent caused by an acquisition made by the Company in accordance with *Section 6.1(d)* and (iii) any adverse effect to the extent caused by an acquisition made by Parent in accordance with *Section 7.14*. As used in this Agreement, the term "*subsidiary*" of a person shall mean any corporation or other entity (including partnerships and other business associations) of which a majority of the outstanding capital stock or other voting securities having voting power under ordinary circumstances to elect directors or similar members of the governing body of such corporation or entity shall at the time be held, directly or indirectly, by such person. True, accurate and complete copies of the certificate of incorporation and by-laws of the Company (including any amendments thereto) as in effect on the date hereof have been made available to Parent.

SECTION 4.2 ***Subsidiaries.*** Section 4.2 of the Company Disclosure Schedule sets forth a description as of the date hereof, of (x) all "material subsidiaries" of the Company as defined in Regulation S-X promulgated under the Securities Act (as defined herein) and (y) all other subsidiaries and joint ventures of the Company, including (i) the name of each such entity, (ii) the state or jurisdiction of its incorporation or organization, (iii) the Company's interest therein, and (iv) if known by the Company, the name of any other person holding an interest therein and the interest held by any and all such persons, and a brief description of the principal line or lines of business conducted by each such entity. Except as set forth in Section 4.2 of Company Disclosure Schedule, neither the Company nor any of the Company's subsidiaries is a "public utility company" or a "holding company" within the meaning of Section 2(a)(5) or 2(a)(7) of the Public Utility Holding Company Act of 1935, as amended (the "*1935 Act*") or a "subsidiary company" or an "affiliate" within the meaning of Section 2(a)(8) or 2(a)(11) of the 1935 Act of any holding company which is required to register as a holding company under the 1935 Act. Except as set forth in Section 4.2 of the Company Disclosure Schedule, all of the issued and outstanding shares of capital stock of each subsidiary of the Company and, to the knowledge of the Company, each Company Joint Venture (as defined below) are validly issued, fully paid, nonassessable and free of preemptive rights, and are owned, directly or indirectly, by the Company free and clear of any liens, claims, encumbrances, security interests, equities, charges and options of any nature whatsoever and there are no outstanding subscriptions, options, calls, contracts, voting trusts, proxies or other commitments, understandings, restrictions, arrangements, rights or warrants, including any right of conversion or exchange under any outstanding security, instrument or other agreement, obligating any such subsidiary to issue, deliver or sell, or cause to be issued, delivered or sold, additional shares of its capital stock or obligating it to grant, extend or enter into any such agreement or commitment, except for any of the foregoing that could not reasonably be expected to have a Company Material Adverse Effect. As used in this Agreement, the term "*joint venture*" of a person shall mean any corporation or other entity (including partnerships and other business associations) that is not a subsidiary of such person, in which such person or one or more of its subsidiaries owns an equity interest, other than equity interests held for passive investment purposes which are less than 10% of any class of the outstanding voting securities or equity of any such entity, and the term "*Company Joint Venture*" shall mean each joint venture in which the Company holds an equity interest and in which neither Parent nor any of Parent's affiliates holds a direct or indirect equity interest apart from their interest in the Company.

SECTION 4.3 ***Capitalization.*** (a) *Company Capitalization.* The authorized capital stock of the Company consists of (i) 100,000,000 shares of Company Common Stock, (ii) 1,000,000 shares of preferred stock, no par value, of the Company (the "*Company Preferred Stock*"), and (iii) 5,000,000 shares of preference stock, no par value, of the Company (the "*Company Preference Stock*") of which 3,983,976 shares are designated as Series A Preference Stock and no shares are designated as 7 5/8% Series B Cumulative Preferred Stock, no par value, of the Company ("*Series B Preferred Stock*"). As of the close of business on July 17, 1999, there were issued and outstanding 38,810,209 shares of Company Common Stock, 1,956,596 shares of Series A Preference Stock and no shares of Series B Preferred Stock. All of the issued and outstanding shares of the capital stock of the Company are validly issued, fully paid, nonassessable and free of preemptive rights.

(b) *Options, etc.* Except as set forth in Section 4.3(b) of the Company Disclosure Schedule, as of the date hereof, there are no outstanding subscriptions, options (including employee stock options), calls, contracts, voting trusts, proxies or other commitments, understandings, restrictions, arrangements, rights (including the Rights) or warrants, including any right of conversion or exchange under any outstanding security, instrument or other agreement, obligating the Company or any of the subsidiaries of the Company or, to the knowledge of the Company, any Company Joint Venture to issue, deliver or sell, or cause to be issued, delivered or sold, additional shares of the capital stock of such person, or obligating such person to grant, extend or enter into any such agreement or commitment. The total number of outstanding options to purchase shares of Company's capital stock (whether granted pursuant to Company Stock Plans or otherwise) and the exercise price of each such option is set forth on Section 4.3(b) of the Company Disclosure Schedule.

(c) *Certain Contractual Obligations.* There are no outstanding contractual obligations of the Company, any of its subsidiaries or, to the knowledge of the Company, any Company Joint Venture to repurchase, redeem or otherwise acquire any shares of such person's capital stock or to provide funds to, or make any investment (in the form of a loan, capital contribution or otherwise) in, any person other than to subsidiaries of the Company in the ordinary course of business consistent with past practice or as disclosed in Section 4.3(c) of the Company Disclosure Schedule.

SECTION 4.4 ***Authority; Non- Contravention; Statutory Approvals; Compliance.***

(a) *Authority.* The Company has all requisite corporate power and authority (including approval of the Company's Board of Directors) to enter into this Agreement, to perform its obligations hereunder and, subject to obtaining the Company Stockholders' Approval (as defined in *Section 4.14*) and the Company Required Statutory Approvals (as defined in *Section 4.4(c)*), to consummate the transactions contemplated hereby. The execution, delivery and performance of this Agreement and the consummation by the Company of the transactions contemplated hereby have been duly authorized by all necessary corporate action on the part of the Company, subject to obtaining the Company Stockholders' Approval with respect to consummation of the Merger. This Agreement has been duly and validly executed and delivered by the Company and, assuming the due authorization, execution and delivery hereof by the other signatories hereto, constitutes the valid and binding obligation of the Company enforceable against it in accordance with its terms.

(b) *Non-Contravention.* Except as set forth in Section 4.4(b) of the Company Disclosure Schedule, the execution and delivery of this Agreement by the Company does not, and the performance by the Company of its obligations hereunder and the consummation of the transactions contemplated hereby will not, violate, conflict with, or result in a breach of any provision of, or constitute a default (with or without notice or lapse of time or both) under, or result in the termination or modification of, or accelerate the performance required by, or result in a right of termination, cancellation, or acceleration of any obligation or the loss of a benefit under, or result in the creation of any lien, security interest, charge or encumbrance ("*Liens*") upon any of the properties or assets of the Company or any of the subsidiaries of the Company or, to the knowledge of the Company, any of the Company Joint Ventures (any such violation, conflict, breach, default, right of termination, modification, cancellation or acceleration, loss or creation, a "*Violation*" with respect to the Company (such term when used in *Article V* having a correlative meaning with respect to Parent)) pursuant to any terms, conditions or provisions of (i) the certificate of incorporation, by-laws or similar governing documents of the Company or any of its subsidiaries or, to the knowledge of the Company, any of the Company Joint Ventures, (ii) subject to obtaining the Company Required Statutory Approvals and the receipt of the Company Stockholders' Approval, any statute, law, ordinance, rule, regulation, judgment, decree, order, injunction, writ, permit or license of any Governmental Authority (as defined in *Section 4.4(c)*) applicable to the Company or any of its subsidiaries or, to the knowledge of the Company, any of the Company Joint Ventures, or any of their respective properties or assets or (iii) subject to obtaining the third-party consents or other approvals set forth in Section 4.4(b) of the Company Disclosure Schedule (the "*Company Required Consents*") any note, bond, mortgage, indenture, deed of trust, license, franchise, permit, concession, contract, lease or other instrument, obligation or agreement of any kind to which the Company or any of its subsidiaries or, to the knowledge of the Company, any of the Company Joint Ventures is a party or by which the Company or any of the Company's, its subsidiaries' or any Company Joint Venture's properties or assets may be bound or affected, excluding from the foregoing clauses (ii) and (iii) such Violations as would not reasonably be likely to have, individually or in the aggregate, a Company Material Adverse Effect.

(c) *Statutory Approvals.* No declaration, filing or registration with, or notice to or authorization, consent or approval of, any court, federal, state, local or foreign governmental or regulatory body (including a stock exchange or other self-regulatory body) or authority, including state public utility control or public service commissions and similar state regulatory bodies (each, a "*Governmental Authority*") is necessary for the execution and delivery of this Agreement by the Company, the performance of the Company of its obligations hereunder or the consummation by the Company of the transactions contemplated hereby, except as described in Section 4.4(c) of the Company Disclosure Schedule, the failure to obtain, make or give which would reasonably be likely to have, individually or in the aggregate, a Company Material Adverse Effect (the "*Company Required Statutory Approvals*"), it being understood that references in this Agreement to "obtaining" such Company Required Statutory Approvals shall mean making such declarations, filings or registrations, giving such notices, obtaining such authorizations, consents or approvals and having such waiting periods expire as are necessary to avoid a violation of law.

(d) *Compliance.* Except as set forth in Section 4.4(d) or Section 4.11 of the Company Disclosure Schedule, or as disclosed in the Company SEC Reports (as defined in *Section 4.5*) filed prior to the date hereof, neither the Company nor any of its subsidiaries nor, to the knowledge of the Company, any Company Joint Venture is in violation of, is under investigation with respect to any violation of, or has been given notice or been charged with any violation of, any law, statute, order, rule, regulation, ordinance or judgment of any Governmental Authority except for violations that, individually or in the aggregate, do not have, and to the knowledge of the Company, are not reasonably likely to have, a Company Material Adverse Effect. Except as set forth in Section 4.4(d) of the Company Disclosure Schedule or in Section 4.11 of the Company Disclosure Schedule, the Company and its subsidiaries and, to the knowledge of the Company, the Company Joint Ventures have all permits, licenses, franchises and other governmental authorizations, consents and approvals necessary to conduct their respective businesses as currently conducted in all respects, except those which the failure to obtain would, in the aggregate, not have a Company Material Adverse Effect. Except as set forth in Section 4.4(d) of the Company Disclosure Schedule, the Company, each of its subsidiaries and, to the knowledge of the Company, each Company Joint Venture is not in breach or violation of or in default in the performance or observance of any term or provision of, and no event has occurred which, with lapse of time or action by a third party, could result in a default under, (i) its certificate of incorporation or by-laws or similar organizational documents or (ii) any material contract, commitment, agreement, indenture, mortgage, loan agreement, note, lease, bond, license, approval or other instrument to which it is a party or by which it is bound or to which any of its property is subject, except for breaches, violations or defaults of any of the foregoing items in clause (ii) that, individually or in the aggregate, do not have, and are not reasonably likely to have, a Company Material Adverse Effect.

SECTION 4.5 ***Reports and Financial Statements.*** The filings required to be made by the Company and its subsidiaries under the Securities Act of 1933, as amended (the "*Securities Act*"), the Securities Exchange Act of 1934, as amended (the "*Exchange Act*"), and applicable state public utility laws and regulations have been filed with the Securities and Exchange Commission (the "*SEC*"), or the appropriate state public utilities commission or health agency, as the case may be, including all forms, statements, reports, agreements (oral or written) and all documents, exhibits, amendments and supplements appertaining thereto, and complied, as of their respective dates, in all material respects with all applicable requirements of the appropriate statute and the rules and regulations thereunder. The Company has made available to Parent a true and complete copy of each report, schedule, registration statement and definitive proxy statement filed by the Company with the SEC since June 30, 1996 (as such documents have since the time of their filing been amended, the "*Company SEC Reports*"). As of their respective dates, the Company SEC Reports did not contain any untrue statement of a material fact or omit to state a material fact required to be stated therein or necessary to make the statements therein, in light of the circumstances under which they were made, not misleading. The audited consolidated financial statements and unaudited interim financial statements of the Company included in the Company SEC Reports (collectively, the "*Company Financial Statements*") have been prepared in accordance with generally accepted accounting principles applied on a consistent basis ("*GAAP*") (except as may be indicated therein or in the notes thereto and except with respect to unaudited statements as permitted by Form 10-Q of the SEC) and fairly present the consolidated financial position of the Company as of the dates thereof and the consolidated results of operations and cash flows for the periods then ended. Except as and to the extent set forth in the Company Financial Statements, neither the Company nor any subsidiary of the Company or, to the knowledge of the Company, any Company Joint Venture has any liability or obligation of any nature (whether accrued, absolute, contingent or otherwise) which would be required to be reflected on a balance sheet prepared in accordance with generally accepted accounting principles, except for liabilities and obligations that would not reasonably be likely to have, individually or in the aggregate, a Company Material Adverse Effect.

SECTION 4.6 ***Absence of Certain Changes or Events.*** Except as disclosed in the Company SEC Reports filed prior to the date hereof or as set forth in Section 4.6 of the Company Disclosure Schedule, from June 30, 1999, the Company and each of its subsidiaries have conducted their business only in the ordinary course of business consistent with past practice and there has not been, and no fact or condition exists which would, individually or in the aggregate, have a Company Material Adverse Effect. Without limiting the foregoing, from June 30, 1999 through the date of this Agreement, and except as which individually or in the aggregate, does not have or, insofar as reasonably can be foreseen, is not reasonably likely to have a Company Material Adverse Effect, there has not been (i) any revaluation by the Company or any of its subsidiaries or, to the knowledge of the Company, any Company Joint Venture of any of their respective assets, including, but not limited to, write-offs of accounts receivable, other than in the ordinary course of businesses consistent with historical practices, (ii) any material change by the Company, any of its subsidiaries or, to the knowledge of the Company, any Company Joint Venture in its accounting methods, principles or practices, or (iii) any declaration, setting aside or payment of any dividend or distribution in respect of any capital stock of the Company or any redemption, repurchase or other acquisition of any of its securities (other than regular quarterly dividends on the shares of Company Common Stock and regular dividends on the shares of Series A Preference Stock).

SECTION 4.7 ***Litigation.*** Except as disclosed in the Company SEC Reports filed prior to the date hereof or as set forth in Section 4.7, Section 4.9 or Section 4.11 of the Company Disclosure Schedule, (i) there are no claims, suits, actions or proceedings, pending or, to the knowledge of the Company, threatened, nor are there, to the knowledge of the Company, any investigations or reviews pending or threatened against, relating to or affecting the Company or any of its subsidiaries or any Company Joint Venture and (ii) there are no judgments, decrees, injunctions, rules or orders of any court, governmental department, commission, agency, instrumentality or authority or any arbitrator applicable to the Company, any of its subsidiaries or, to the knowledge of the Company, any Company Joint Venture, except for any of the foregoing under clauses (i) and (ii) that individually or in the aggregate would not reasonably be expected to have a Company Material Adverse Effect.

SECTION 4.8 ***Proxy Statement Etc.*** The proxy statement, in definitive form, relating to the Company Special Meeting (the "*Proxy Statement*") shall not, at the dates mailed to stockholders and at the time of the Company Special Meeting, contain any untrue statement of a material fact or omit to state any material fact required to be stated therein or necessary in order to make the statements therein in light of the circumstances under which they are made, not misleading. The Proxy Statement, insofar as it relates to the Company or any subsidiary of the Company, shall comply as to form in all material respects with the applicable provisions of the Securities Act and the Exchange Act and the rules and regulations thereunder.

SECTION 4.9 *Tax Matters.* "*Taxes*", as used in this Agreement, means any federal, state, county, local or foreign taxes, charges, fees, levies or other assessments, including all net income, gross income, sales and use, *ad valorem*, transfer, gains, profits, excise, franchise, real and personal property, gross receipts, capital stock, production, business and occupation, disability, employment, alternative minimum, payroll, license, estimated, stamp, custom duties, severance or withholding taxes or charges imposed by any governmental entity, and includes any interest and penalties (civil or criminal) on or additions to any such taxes and any expenses incurred in connection with the determination, settlement or litigation of any tax liability. "*Tax Return*", as used in this Agreement, means a report or similar statement, return or other information required to be supplied to a governmental entity with respect to Taxes including, where permitted or required, combined or consolidated returns for any group of entities that includes the Company or any of its subsidiaries, or Parent or any of its subsidiaries, as the case may be.

Except as set forth in Section 4.9 of the Company Disclosure Schedule:

(a) *Timely Filing of Tax Returns.* The Company and each of its subsidiaries and, to the Company's knowledge, each Company Joint Venture have filed (or there has been filed on its behalf) all material Tax Returns required to be filed by each of them under applicable law. All such Tax Returns were and are in all material respects true, complete and correct and filed on a timely basis.

(b) *Payment of Taxes.* The Company and each of its subsidiaries and, to the Company's knowledge, each Company Joint Venture have, within the time and in the manner prescribed by law, paid all Taxes that are currently due and payable except for those contested in good faith and for which adequate reserves have been taken.

(c) *Deferred Taxes.* The Company and each of its subsidiaries and, to the Company's knowledge, each Company Joint Venture have accounted for deferred income taxes in accordance with GAAP.

(d) *Tax Liens.* There are no Tax liens upon the assets of the Company or any of its subsidiaries or, to the Company's knowledge, any Company Joint Venture except liens for Taxes not yet due.

(e) *Withholding Taxes.* The Company and each of its subsidiaries and, to the Company's knowledge, each Company Joint Venture have complied in all material respects with the provisions of the Code relating to the withholding of Taxes, as well as similar provisions under any other laws, and have, within the time and in the manner prescribed by law, withheld from employee wages and paid over to the proper governmental authorities all amounts required.

(f) *Extensions of Time for Filing Tax Returns.* Neither the Company nor any of its subsidiaries nor, to the Company's knowledge, any Company Joint Venture has requested any extension of time within which to file any Tax Return which Tax Return has not since been filed.

(g) *Waivers of Statute of Limitations.* Neither the Company nor any of its subsidiaries nor, to the Company's knowledge, any Company Joint Venture has executed any outstanding waivers or comparable consents regarding the application of the statute of limitations with respect to any Taxes or Tax Returns.

(h) *Expiration of Statute of Limitations.* The statute of limitations for the assessment of all Taxes has expired for all applicable Tax Returns of the Company and each of its subsidiaries and, to the Company's knowledge, each Company Joint Venture, or those Tax Returns have been examined by the appropriate taxing authorities for all periods through the date hereof, and no deficiency for any Taxes has been proposed, asserted or assessed against the Company or any of its subsidiaries or, to the Company's knowledge, any Company Joint Venture that has not been resolved and paid in full.

(i) *Audit, Administrative and Court Proceedings.* No audits or other administrative proceedings or court proceedings are presently pending, proposed or threatened with regard to any Taxes or Tax Returns of the Company or any of its subsidiaries or, to the Company's knowledge, any Company Joint Venture.

(j) *Powers of Attorney.* No power of attorney currently in force has been granted by the Company or any of its subsidiaries or, to the Company's knowledge, any Company Joint Venture concerning any Tax matter.

(k) *Tax Rulings.* Neither the Company nor any of its subsidiaries nor, to the Company's knowledge, any Company Joint Venture has received a Tax Ruling (as defined below) or entered into a Closing Agreement (as defined below) with any taxing authority that would have a continuing adverse effect after the Closing Date. "*Tax Ruling*", as used in this Agreement, shall mean a written ruling of a taxing authority relating to Taxes. "*Closing Agreement*", as used in this Agreement, shall mean a written and legally binding agreement with a taxing authority relating to Taxes.

(l) *Availability of Tax Returns.* The Company has made or has used its best efforts in making available to Parent complete and accurate copies of (i) all Tax Returns, and any amendments thereto, filed by the Company or any of its subsidiaries since December 31, 1997, (ii) all audit reports received from any taxing authority relating to any Tax Return filed by the Company or any of its subsidiaries or, to the Company's knowledge, any Company Joint Venture and (iii) any Closing Agreements entered into by the Company or any of its subsidiaries or, to the Company's knowledge, any Company Joint Venture with any taxing authority.

(m) *Tax Sharing Agreements.* Neither the Company nor any of its subsidiaries nor, to the Company's knowledge, any Company Joint Venture is a party to any agreement relating to allocating or sharing of Taxes.

(n) *Code Section 280G.* Section 4.9 of the Company Disclosure Schedule contains a true and complete list of any agreement, contract or arrangement to which the Company or any of its subsidiaries or, to Company's knowledge, any Company Joint Venture, is a party that could result, on account of the transactions contemplated hereunder, separately or in the aggregate, in the payment of any "excess parachute payments" within the meaning of Section 280G of the Code.

(o) *Liability for Others.* Neither the Company nor any of its subsidiaries nor, to the Company's knowledge, any Company Joint Venture has any liability for Taxes of any person other than the Company, its subsidiaries and, to the Company's knowledge, such Company Joint Ventures (i) under Treasury Regulations Section 1.1502-6 (or any similar provision of state, local or foreign law) as a transferee or successor, (ii) by contract or (iii) otherwise.

(p) *Code Section 897.* To the Company's knowledge after due inquiry, no foreign person owns or has owned, for purposes of Section 897 of the Code, more than five percent of the total fair market value of the Company Common Stock during the applicable period specified in Section 897(c)(1)(A)(ii) of the Code, and, at all times during the applicable period specified in Section 897(c)(1)(A)(ii) of the Code, the Company Common Stock has been regularly traded in an established securities market within the meaning of Treasury Regulation Section 1.897-1(m).

SECTION 4.10 ***Employee Matters; ERISA.*** Except as set forth in Section 4.10 of the Company Disclosure Schedule:

(a) *Benefit Plans.* Section 4.10(a) of the Company Disclosure Schedule contains a true and complete list of each material employee benefit plan sponsored, contributed to or maintained by the Company or any of its subsidiaries covering employees, former employees, directors or former directors of the Company or any of its subsidiaries or their beneficiaries, or providing benefits to such persons in respect of services provided to any such entity, including, but not limited to, any employee benefit plans within the meaning of Section 3(3) of the Employee Retirement Income Security Act of 1974, as amended ("*ERISA*"), and any severance or change in control agreement between the Company or any of its subsidiaries and any current or former employee or director thereof pursuant to which benefits may become payable (collectively, the "*Company Benefit Plans*"). No Company Benefit Plan is a "multiemployer plan" as defined in Section 3(37) of ERISA. There are no trades or businesses which, together with the Company and its subsidiaries, would be treated as a "single employer" within the meaning of Section 414 of the Code or Section 4001(a)(14) of ERISA (''*ERISA Affiliates*''), except as set forth on Section 4.10(a) of the Company Disclosure Schedule. Except as disclosed in Section 4.10(a) of the Company Disclosure Schedule, no ERISA Affiliates sponsor, maintain or contribute to any employee benefit plan subject to Title IV of ERISA or Section 412 of the Code.

(b) *Contributions.* All material contributions and other payments required to be made for any period through the date to which this representation speaks, by the Company or any of its subsidiaries to any Company Benefit Plan (or to any person pursuant to the terms thereof) have been timely made or paid in full or, to the extent not required to be made or paid on or before the date to which this representation speaks have been reflected in the Company Financial Statements.

(c) *Qualification; Compliance.* Each of the Company Benefit Plans intended to be ''qualified'' within the meaning of Section 401(a) of the Code has received from the Internal Revenue Service (the ''*IRS*'') a determination letter that the plan is qualified with respect to all applicable provisions of the Code for which the applicable remedial amendment period has expired or an application for such a determination, which was filed before the expiration of the applicable remedial amendment period, is pending, and, to the knowledge of the Company, no circumstances exist that could reasonably be expected to result in the revocation of any such determination, and each trust forming a part of any such plan is exempt from federal income tax pursuant to Section 501(a) of the Code. The Company and each of its subsidiaries is in compliance with, and each of the Company Benefit Plans is and has been operated in compliance with, the terms of such plans and all applicable laws, rules and regulations governing such plan, including, without limitation, ERISA and the Code, except where failure to so comply would not reasonably be likely to have, individually or in the aggregate, a Company Material Adverse Effect. There are no pending or, to the knowledge of the Company, threatened claims under or in respect of any Company Benefit Plan by or on behalf of any employee, former employee, director, former director, or beneficiary thereof, or otherwise involving any Company Benefit Plan (other than routine claims for benefits).

(d) *Title IV Liabilities.* No event has occurred and, to the knowledge of the Company, there exists no condition or set of circumstances, that could subject or potentially subject the Company or any of its subsidiaries to any liability arising under or based upon any provision of Title IV of ERISA (whether to a governmental agency, a multiemployer plan or to any other person or entity) which could reasonably be expected to have a Company Material Adverse Effect.

(e) *Documents Made Available.* The Company has made available to Parent a true and correct copy of each collective bargaining agreement to which the Company or any of its subsidiaries is a party or under which the Company or any of its subsidiaries has obligations and, with respect to each Company Benefit Plan, where applicable, (i) such plan and the most recent summary plan description, (ii) the most recent annual report filed with the IRS, (iii) each related trust agreement or insurance contract, (iv) the most recent determination of the IRS with respect to the qualified status of such Company Benefit Plan, and (v) the most recent actuarial report or valuation.

(f) *Labor Agreements.* Except as disclosed in Section 4.10(f) of the Company Disclosure Schedule, neither the Company nor any of its subsidiaries is a party to any collective bargaining agreement or other labor agreement with any union or labor organization. To the best knowledge of the Company, there is no current union representation question involving employees of the Company or any of its subsidiaries, nor does the Company know of any activity or proceeding of any labor organization (or representative thereof) or employee group to organize any such employees. Except as disclosed in the Company SEC Reports filed prior to the date hereof or in Section 4.10(f) of the Company Disclosure Schedule, (i) there is no unfair labor practice, employment discrimination or other material complaint against the Company or any of its subsidiaries pending or, to the best knowledge of the Company, threatened, (ii) there is no strike or lockout or material dispute, slowdown or work stoppage pending, or to the best knowledge of the Company, threatened, against or involving the Company, and (iii) there is no proceeding, claim, suit, action or governmental investigation pending or, to the best knowledge of the Company, threatened, in respect of which any director, officer, employee or agent (or, except as disclosed in Section 4.10(f) of the Company Disclosure Schedule, any former director, officer, employee or agent) of the Company or any of its subsidiaries are or may be entitled to claim indemnification from the Company or such subsidiary pursuant to their respective certificates of incorporation or by-laws or as provided in the indemnification agreements listed in Section 4.10(f) of the Company Disclosure Schedule.

(g) Except as required by law or as would not reasonably be likely to have, individually or in the aggregate, a Company Material Adverse Effect, no Company Benefit Plan provides retiree medical or retiree life insurance benefits to any person except as disclosed in Section 4.10(g) of the Company Disclosure Schedule. The accumulated post-retirement benefit obligation of the Company and its subsidiaries (as determined under FASB Statement No. 106) as of December 31, 1998 does not exceed $6,400,000.

(h) Except as disclosed in Section 4.10(h) of the Company Disclosure Schedule, no director or officer or other employee of the Company or its subsidiaries will become entitled to any retirement, severance or similar benefit or enhanced or accelerated benefit solely as a result of the transactions contemplated hereby. Except as disclosed on Schedule 4.10(h) of the Company Disclosure Schedule, such benefit would not be an "excess parachute payment" to a "disqualified individual" as those terms are defined in Code Section 280G.

(i) Except as disclosed on Section 4.10(i) of the Company Disclosure Schedule, since June 30, 1999, there has been no change in the terms and conditions of employment of any director or any of the fifteen most senior officers of the Company.

(j) There has been no amendment to, written interpretation of or announcement (whether or not written) by the Company or any of its subsidiaries relating to, or change in employee participation or coverage under, any Company Benefit Plan which would increase materially the expense of maintaining such plan above the level of expense incurred in respect thereto for the most recent 12 month period updated on the Company Financial Statements except as set forth in Section 4.10(i) of the Company Disclosure Schedule.

SECTION **4.11** ***Environmental Protection.*** Except as set forth in Section 4.11 of the Company Disclosure Schedule or in the Company SEC Reports filed prior to the date hereof:

(a) *Compliance.* The Company and to the Company's knowledge each of its subsidiaries are in compliance with all Environmental Laws and the Company has not received any communication from any Governmental Authority or third party that alleges that the Company or any of its subsidiaries is not in compliance with applicable Environmental Laws, except where the failure to be in such compliance would not reasonably be likely to have, individually or in the aggregate, a Company Material Adverse Effect. The Company has made available to Parent copies of any and all material environmental assessment or audit reports or other similar studies or analyses generated within the last three years and in Company's possession, that relate to the Company or any of its subsidiaries or the Company Joint Ventures.

(b) *Environmental Permits.* The Company and to the Company's knowledge each of its subsidiaries have obtained all applicable environmental, health and safety permits, licenses, approvals and governmental authorizations (collectively, the "*Environmental Permits*") which are required, pursuant to Environmental Laws, for the construction of their facilities and the conduct of their operations; all such Environmental Permits are in current effect and in good standing; all required renewal applications have been timely filed and are pending agency approval; the Company reasonably believes that such renewals will be accomplished in the ordinary course of business without material delay or expense (except where failure to accomplish such renewals would not, individually or in the aggregate, be reasonably likely to have a Company Material Adverse Effect); and the Company has received no information that when renewed such permit(s) will impose material restrictions or obligations not required in the current permit; no capital expense will be required to meet the requirements of any permit or Environmental Law existing as of the date hereof except for such capital expenditure as would not reasonably be likely to have, individually or in the aggregate, a Company Material Adverse Effect; the Company and its subsidiaries are in compliance with all terms and conditions of the Environmental Permits, except for such noncompliance as would not reasonably be likely to have, individually or in the aggregate, a Company Material Adverse Effect; the Company reasonably believes that any transfer or renewal of or reapplication for any Environmental Permit required as a result of the Merger can be accomplished in the ordinary course of business without material delay or expense (except where failure to accomplish such transfer or renewal will not, individually or in the aggregate, be reasonably likely to have a Company Material Adverse Effect).

(c) *Environmental Claims.* There is no Environmental Claim pending or, to the best knowledge of the Company, threatened against the Company or any of its subsidiaries that, if adversely determined, would have, individually or in the aggregate, a Company Material Adverse Effect. There are no circumstances existing, to the knowledge of the Company, that would form a reasonable basis for an Environmental Claim against the Company or any of its subsidiaries which, if adversely determined, would have, individually or in the aggregate, a Company Material Adverse Effect. To the Company's knowledge, no real property currently or formerly owned or operated by the Company or any subsidiary is listed on the National Priorities List, the CERCLIS or any state or local list of sites with known or suspected Release.

(d) *Releases.* The Company has no knowledge of any Releases that would be reasonably likely to form the basis of any Environmental Claim against the Company or any of its subsidiaries, except for Releases the liability for which would not reasonably be likely to have, individually or in the aggregate, a Company Material Adverse Effect.

(e) *Predecessors.* The Company has no knowledge of any Environmental Claim pending or of any Release that would be reasonably likely to form the basis of any Environmental Claim, in each case against any predecessor of the Company or any of its subsidiaries or any other party whose liability the Company or any of its subsidiaries has or may have retained or assumed either contractually or by operation of law, except for such Releases the liability for which would not, individually or in the aggregate, have a Company Material Adverse Effect.

(f) *As used in this Agreement:*

(i) "*Environmental Claim*" means any and all administrative, regulatory or judicial actions, suits, demands, demand letters, directives, claims, liens, investigations, proceedings or notices of noncompliance or violation by any person or by any Governmental Authority with jurisdiction under Environmental Laws alleging potential responsibility or liability for enforcement costs, investigatory costs, cleanup costs, governmental response costs, removal costs, remedial costs, natural-resources damages, property damages, personal injuries, fines or penalties, or other liabilities pursuant to Environmental Laws including, but not limited to those arising out of, based on or resulting from (A) the presence of any Hazardous Materials or (B) circumstances forming the basis of any violation, or alleged violation, of any Environmental Law.

(ii) "*Environmental Laws*" means any applicable statute, regulation, rule, code, common law, order or judgment of any federal, state, local or foreign jurisdiction where the Company or any of its subsidiaries operates concerning protection or preservation of the environment, human health or natural resources, including but not limited to statutes, regulations, rules, codes, common law, orders or judgments relating to (i) any discharges, releases or emissions to air, water (including surface water, ground water and wetlands), soil or sediment, (ii) the quality of any environmental medium, (iii) the generation, treatment, recycling, storage, disposal, transportation or other management of waste, (iv) the manufacture, distribution, disposal, or recycling of chemical substances and mixtures, or (v) responsibility or liability for environmental conditions.

(iii) "*Hazardous Materials*" means any substance, material or waste (in any relevant physical form or concentration) regulated, listed or identified under any Environmental Law and any other substance, material or waste (in any form or concentration) which is hazardous, dangerous, or toxic to living things or the environment.

(iv) "*Release*" means any spilling, leaking, pumping, pouring, emitting, emptying, discharging, injecting, escaping, leaching, dumping or disposing into the environment of any Hazardous Materials.

SECTION 4.12 ***Regulation as a Utility.*** The Company and/or its subsidiaries are regulated as a public utility in the states set forth on Section 4.12 of the Company Disclosure Schedule. Except as set forth on Section 4.12 of Company Disclosure Schedule, neither the Company nor any "subsidiary company" or "affiliate" of the Company is subject to regulation as a public utility or public service company (or similar designation) by the United States or any other state of the United States. All filings required to be made by the Company or any of its subsidiaries since December 31, 1998, under any applicable laws or orders relating to the regulation of public utilities, have been filed with the appropriate public utility commission, health agency or other appropriate governmental entity (including, without limitation, to the extent required, the state public utility regulatory agencies in the states identified in Section 4.12 of the Company Disclosure Schedule), as the case may be, including all forms, statements, reports, agreements (oral or written) and all documents, exhibits, amendments and supplements appertaining thereto, including but not limited to all rates, tariffs, franchises, service agreements and related documents and all such filings complied, as of their respective dates, with all applicable requirements of the appropriate laws or orders, except for such filings or such failure to comply that would not reasonably be likely to have, individually or in the aggregate, a Company Material Adverse Effect. Except as specified on Section 4.12 of the Company Disclosure Schedule, no approval of any public utilities regulatory authority (including all public utility control or public service commissions and similar state regulatory bodies) is required for the Company's execution and delivery of this Agreement by the Company or the performance of its obligations under this Agreement or the consummation of the transactions contemplated by this Agreement.

SECTION 4.13 ***Water Quality.*** Except as set forth on Section 4.13 of the Company Disclosure Schedule, the quality of water supplied by the Company and its subsidiaries meets or exceeds all standards for quality and safety of water in all material respects in accordance with all applicable federal, state, local or foreign statutes, laws, ordinances, rules and regulations.

SECTION 4.14 ***Vote Required.*** The approval of (i) two-thirds of the outstanding shares of Company Common Stock not owned by Parent or any affiliate of Parent which is an "interested shareholder" as defined in NJBCA § *14A:10A-3* and (ii) two-thirds of the outstanding shares of the Series A Preference Stock at the Company Special Meeting (collectively, the "*Company Stockholders' Approval*") are the only votes of the holders of any class or series of the capital stock of the Company or any of its subsidiaries required to approve this Agreement, the Merger and the other transactions contemplated hereby.

SECTION 4.15 ***Opinion of Financial Advisor.*** The Company has received the opinion of Morgan Stanley & Co. Incorporated to the effect that, as of the date hereof, the Per Share Cash Consideration is fair from a financial point of view to the holders of Company Common Stock.

SECTION 4.16 ***The Company Rights Agreement.*** The Company has taken all necessary action with respect to all of the outstanding stock purchase rights of the Company (the "*Rights*") issued pursuant to the Rights Agreement, dated as of July 12, 1989, as amended by Amendment No. 1 thereto dated as of September 15, 1993, Amendment No. 2 thereto dated as of July 30, 1999 and Amendment No. 3 thereto dated as of August 20, 1999 (the "*Rights Agreement*"), between the Company and ChaseMellon Shareholder Services, LLC, as Rights Agent, so that the Company, as of the time immediately prior to the Effective Time, will have no obligations under the Rights or the Rights Agreement and so that the holders of the Rights will have no rights under the Rights or the Rights Agreement. The Board of Directors of the Company has taken all necessary action to amend the Rights Agreement so that neither the execution and delivery of this Agreement, the performance of the parties' obligations hereunder nor the consummation of the Merger will (a) cause the

Rights issued pursuant to the Rights Agreement to become exercisable, (b) cause Parent or Merger Sub to become an Acquiring Person (as such term is defined in the Rights Agreement) or (c) give rise to a Distribution Date (as such term is defined in the Rights Agreement). The execution, delivery and performance of this Agreement will not result in a distribution of, or otherwise trigger, the Rights under the Rights Agreement.

SECTION 4.17 ***Real Property.*** The Company and each of its subsidiaries and, to the Company's knowledge, each of the Company Joint Ventures has good title or valid leases with respect to all of their real property free and clear of any and all liens, claims and encumbrances other than (i) as set forth in Section 4.17 of the Company Disclosure Schedule, (ii) those reflected or reserved against in the Company Financial Statements and the notes thereto, (iii) imperfections of title, easements, pledges, charges, restrictions and encumbrances, including, without limitation, survey matters and mechanics' liens, if any, that do not materially detract from the value of the property subject thereto, or materially interfere with the manner in which it is currently being used, (iv) taxes and general and special assessments not in default and payable without penalty or interest, and (v) such other liens, claims and encumbrances as would not reasonably be likely to have, individually or in the aggregate, a Company Material Adverse Effect. Except, in each case, as would not, individually or in the aggregate, have a Company Material Adverse Effect, (A) neither the Company nor any of its subsidiaries nor, to the Company's knowledge, any of the Company Joint Ventures has received any notice for assessments for public improvements against the real property and, to the knowledge of the Company and its subsidiaries, no such assessment has been proposed; and (B) neither the Company nor any of its subsidiaries nor, to the Company's knowledge, any of the Company Joint Ventures has received any notice or order by any governmental or other public authority, any insurance company which has issued a policy with respect to any of such properties or any board of fire underwriters or other body exercising similar functions which (i) relates to violations of building, safety, fire or other ordinances or regulations, (ii) claims any defect or deficiency with respect to any of such properties or (iii) requests the performance of any repairs, alterations or other work to or in any of such properties or in the streets bounding the same. Except as set forth in Section 4.17 of the Company Disclosure Schedule or as would not reasonably be likely to have, individually or in the aggregate, a Company Material Adverse Effect, there is no pending condemnation, expropriation, eminent domain or similar proceeding affecting all or any portion of any of such properties and, to the Company's knowledge, no such proceeding is threatened.

SECTION 4.18 ***Property Franchises.*** The Company and each of its subsidiaries owns or has sufficient rights and consents to use under existing franchises, easements, leases, and license agreements all properties, rights and assets necessary for the conduct of their business and operations as currently conducted, except where the failure to own or have sufficient rights and consents to use such properties, rights and assets would not reasonably be likely to have, individually or in the aggregate, a Company Material Adverse Effect.

SECTION 4.19 ***Insurance.*** The Company and each of its subsidiaries is, and has been continuously since at least January 1, 1995, insured with financially responsible insurers in such amounts and against such risks and losses as are customary for companies conducting the business as conducted by the Company and its subsidiaries during such time period. Neither the Company nor any of its subsidiaries has received any notice of cancellation or termination with respect to any material insurance policy of the Company or any of its subsidiaries. All material insurance policies of the Company and each of its subsidiaries are valid and enforceable policies.

SECTION 4.20 ***Trademarks, Patents and Copyrights.*** Except where a failure is not reasonably likely, individually or in the aggregate, to have a Company Material Adverse Effect, the Company and its subsidiaries and, to the Company's knowledge, the Company Joint Ventures own, or possess licenses or other valid rights to use, all patents, patent rights, trademarks, trademark rights, trade names, trade name rights, copyrights, service marks, trade secrets, applications for trademarks and for service marks, know-how and other proprietary rights and information that are material to the business of the Company and its subsidiaries and, to the Company's knowledge, Company Joint Ventures as currently conducted, and the Company is unaware of any assertion or claim challenging the validity of any of the foregoing, other than any assertions or claims which, individually or in the aggregate, are not reasonably likely to have a Company Material Adverse Effect.

The conduct of the business of the Company and its subsidiaries and, to the Company's knowledge, the Company Joint Ventures as currently conducted does not conflict with any patent, patent right, license, trademark, trademark right, trade name, trade name right, service mark or copyright of any third party, other than conflicts that, individually or in the aggregate, would not reasonably be likely to have a Company Material Adverse Effect. To the knowledge of the Company, there are no infringements by any third party of any proprietary rights owned or licensed by or to the Company or any subsidiary which are reasonably likely to have, individually or in the aggregate, a Company Material Adverse Effect.

SECTION 4.21 ***Year 2000.*** Except as would not reasonably be likely to have, individually or in the aggregate, a Company Material Adverse Effect, to the knowledge of the Company, all internal computer systems, computer software, equipment or technology that are material to the business, finances or operations of the Company and its subsidiaries or were sold or licensed to customers of the Company and its subsidiaries are (i) able to receive, record, store, process, calculate, manipulate and output dates from and after January 1, 2000, time periods that include January 1, 2000 and information that is dependent on or relates to such dates or time periods, in the same manner and with the same accuracy, functionality, data integrity and performance as when dates or time periods prior to January 1, 2000 are involved, (ii) able to store and output date information in a manner that is unambiguous as to century and (iii) able to recognize Year 2000 as a leap year.

ARTICLE V

REPRESENTATIONS AND WARRANTIES OF PARENT

Parent represents and warrants to the Company as follows:

SECTION 5.1 ***Organization and Qualification.*** Except as set forth in Section 5.1 of the Parent Disclosure Schedule (as defined in *Section 7.6(ii)*), Parent, Merger Sub and each of Parent's other subsidiaries is a corporation duly organized, validly existing and in good standing under the laws of its jurisdiction of incorporation or organization, has all requisite corporate power and authority, and has been duly authorized by all necessary approvals and orders, to own, lease and operate its assets and properties to the extent owned, leased and operated and to carry on its business as it is now being conducted and is duly qualified and in good standing to do business in each jurisdiction in which the nature of its business or the ownership or leasing of its assets and properties makes such qualification necessary, other than in such jurisdictions where the failure to be so qualified and in good standing will not, when taken together with all other such failures, have a Parent Material Adverse Effect. As used in this Agreement, "*Parent Material Adverse Effect*" means any change, effect, condition or circumstance that will, or is reasonably likely to, have a material adverse effect on Parent's or Merger Sub's ability to consummate the transactions contemplated by this Agreement.

SECTION 5.2 ***Authority; Non-Contravention; Statutory Approvals.*** *Authority.* Each of Parent and Merger Sub has all requisite corporate power and authority to enter into this Agreement and, subject to the applicable Parent Required Statutory Approvals (as defined in *Section 5.2(c)*), to consummate the transactions contemplated hereby. The execution and delivery of this Agreement by Parent and Merger Sub, the performance by Parent and Merger Sub of their respective obligations hereunder and the consummation by Parent and Merger Sub of the transactions contemplated hereby have been duly authorized by all necessary corporate action on the part of Parent and Merger Sub, respectively. This Agreement has been duly and validly executed and delivered by Parent and Merger Sub and, assuming the due authorization, execution and delivery hereof by the other signatories hereto, constitutes the valid and binding obligation of each of Parent and Merger Sub enforceable against each in accordance with its terms.

(b) *Non-Contravention.* Except as set forth in Section 5.2(b) of the Parent Disclosure Schedule, the execution and delivery of this Agreement by Parent and Merger Sub do not, and the consummation of the transactions contemplated hereby will not, result in a Violation pursuant to any provisions of (i) the certificate of incorporation, by-laws or similar governing documents of Parent or Merger Sub, respectively, or any of Parent's other subsidiaries or, to Parent's knowledge, any of its joint ventures, (ii) subject to obtaining the Parent Required Statutory Approvals, any statute, law, ordinance, rule, regulation, judgment, decree, order, injunction, writ, permit or license of any Governmental Authority applicable to Parent, Merger Sub or any of Parent's other subsidiaries or, to Parent's knowledge, any of its joint ventures or any of their respective properties or assets or (iii) subject to obtaining the third-party consents or other approvals set forth in Section 5.2(b) of the Parent Disclosure Schedule (the "*Parent Required Consents*"), any note, bond, mortgage, indenture, deed of trust, license, franchise, permit, concession, contract, lease or other instrument, obligation or agreement of any kind to which Parent, Merger Sub or any of Parent's other subsidiaries or, to Parent's knowledge, any of its joint ventures is a party or by which it or any of their respective properties or assets may be bound or affected, excluding from the foregoing clauses (ii) and (iii) such violations as would not have, in the aggregate, a Parent Material Adverse Effect.

(c) *Statutory Approvals.* Except as described in Section 5.2(c) of the Parent Disclosure Schedule, no declaration, filing or registration with, or notice to or authorization, consent or approval of, any Governmental Authority is necessary for the execution and delivery of this Agreement by Parent or Merger Sub, the performance by Parent or Merger Sub of their respective obligations hereunder or the consummation by Parent or Merger Sub of the transactions contemplated hereby, the failure to obtain, make or give which would reasonably be likely to have, individually and in the aggregate, a Parent Material Adverse Effect (the "*Parent Required Statutory Approvals*"), it being understood that references in this Agreement to "obtaining" such Parent Required Statutory Approvals shall mean making such declarations, filings or registrations; giving such notices; obtaining such authorizations, consents or approvals; and having such waiting periods expire as are necessary to avoid a violation of law.

SECTION 5.3 ***Reports and Financial Statements.*** The audited consolidated financial statements and unaudited interim financial statements of Parent since December 31, 1995 (collectively, the "*Parent Financial Statements*") have been prepared in accordance with generally accepted accounting principles (except as may be indicated therein or in the notes thereto) and fairly present the consolidated financial position of Parent as of the dates thereof and the consolidated results of its operations and cash flows for the periods then ended. True, accurate and complete copies of the certificate of incorporation and by-laws of Parent (including all amendments thereto) as in effect on the date hereof, have been made available to the Company.

SECTION 5.4 ***Proxy Statement.*** None of the information supplied or to be supplied by or on behalf of Parent or Merger Sub for inclusion or incorporation by reference in the Proxy Statement shall, at the dates mailed to the Company stockholders and at the times of the meeting of the Company stockholders to be held in connection with the Merger, contain any untrue statement of a material fact or omit to state any material fact required to be stated therein or necessary in order to make the statements therein, in light of the circumstances under which they are made, not misleading. The Proxy Statement, insofar as it relates to Parent, Merger Sub or any other Parent subsidiary, shall comply as to form in all material respects with the applicable provisions of the Securities Act and the Exchange Act and the rules and regulations thereunder.

SECTION 5.5 ***Ownership of Company Capital Stock.*** Except as set forth in Section 5.5 of the Parent Disclosure Schedule, Parent does not "beneficially own" (as such term is defined for purposes of Section 13(d) of the Exchange Act) any shares of Company Common Stock or Series A Preference Stock.

SECTION 5.6 ***Financing.*** Parent has or will have available, prior to the Effective Time, sufficient cash in immediately available funds to pay all Cash Consideration required to be paid pursuant to Article II hereof and to consummate the Merger and other transactions contemplated hereby.

ARTICLE VI

CONDUCT OF BUSINESS PENDING THE MERGER

SECTION **6.1** ***Covenants of Company.*** After the date hereof and prior to the Effective Time or earlier termination of this Agreement, the Company agrees as to itself and to its subsidiaries, as follows, except as expressly contemplated or permitted in this Agreement, or to the extent Parent shall otherwise consent in writing:

(a) *Ordinary Course of Business.* The Company shall, and shall cause its subsidiaries to, carry on their respective businesses in the usual, regular and ordinary course in substantially the same manner as heretofore conducted. In addition, the Company shall, and shall cause its subsidiaries to, use all commercially reasonable efforts to (i) preserve intact its present business organization and goodwill, preserve the goodwill and relationships with customers, suppliers and others having business dealings with it, (ii) subject to prudent management of workforce needs and ongoing programs currently in force, keep available the services of its present officers and employees as a group, and (iii) maintain and keep material properties and assets in as good repair and condition as at present, subject to ordinary wear and tear, and maintain supplies and inventories in quantities consistent with past practice.

(b) *Dividends.* The Company shall not nor shall it permit any of its subsidiaries to: (i) declare or pay any dividends on or make other distributions in respect of any of their capital stock other than (A) dividends by a wholly-owned subsidiary to the Company or another wholly-owned subsidiary, (B) dividends by a less than wholly-owned subsidiary consistent with past practice, (C) stated dividends on Company Preferred Stock, (D) regular dividends on Company Common Stock with usual record and payment dates that, in any fiscal quarter, do not exceed 100% of the dividends for the same quarter of the prior fiscal year, (E) if the Effective Time occurs on a date other than a usual record date for dividends on Company Common Stock, a "stub period" dividend equal to an amount not to exceed 100% of the dividends for the same quarter of the prior fiscal year as the quarter in which the Effective Time occurs multiplied by a fraction, the numerator of which is the number of days between the immediately preceding record date and the Effective Time and the denominator of which is the number of days between such record date and the next regularly scheduled record date, (F) an additional dividend on Company Common Stock in each of the first three fiscal quarters following the date of this Agreement in an amount not to exceed $0.06 per share per quarter, and (G) a special dividend payable to each holder of record of Company Common Stock immediately prior to the Effective Time in an amount per share equal to the difference between $0.48 and the amount of the aggregate dividends per share payable pursuant to clause (F) of this *Section 6.1(b)*; (ii) split, combine or reclassify any capital stock or the capital stock of any subsidiary or issue or authorize or propose the issuance of any other securities in respect of, in lieu of, or in substitution for, shares of capital stock or the capital stock of any subsidiary; or (iii) redeem, repurchase or otherwise acquire any shares of capital stock or the capital stock of any subsidiary (or any option with respect thereto) other than (A) redemptions, repurchases and other acquisitions of shares of capital stock in connection with the administration of employee benefit and dividend reinvestment plans as in effect on the date hereof in the ordinary course of the operation of such plans consistent with past practice, or (B) the intercompany acquisitions of capital stock described in Section 6.1(b) of the Company Disclosure Schedule.

(c) *Issuance of Securities.* The Company shall not, nor shall it permit any of its subsidiaries to, issue, agree to issue, deliver, sell, award, pledge, dispose of or otherwise encumber or authorize or propose the issuance, delivery, sale, award, pledge, disposal or other encumbrance of, any shares of their capital stock of any class or any securities convertible into or exchangeable for, or any rights, warrants or options to acquire, any such shares or convertible or exchangeable securities, other than as provided for in the Company Benefit Plans consistent with past practice or as set forth in Section 6.1(c) of the Company Disclosure Schedule. The Company shall promptly furnish to Parent such information as may be reasonably requested including financial information. Without limiting the foregoing, as soon as practicable following the date of this Agreement, the Company shall exercise and shall cause any applicable administrator to exercise all discretion to (i) purchase Company Common Stock for participants under its Dividend Reinvestment and Stock Purchase Plan (the "*DRIP Program*") on the open market for all dividend payment dates following the date of this Agreement and terminate the issuance or distribution of shares under the DRIP Program at the earliest possible date; (ii) purchase Company Common Stock for distribution to participants under its Management Incentive Plan and other Company Stock Plans on the open market for all distributions following the date of this Agreement; and (iii) make any and all purchases of Company Common Stock for its 401(k) plan (or other retirement plan) on the open market.

(d) *Acquisitions.* Except as disclosed in Section 6.1(d) of the Company Disclosure Schedule, the Company shall not, nor shall it permit any of its subsidiaries to, acquire or agree to acquire, by merging or consolidating with, or by purchasing a substantial equity interest in or a substantial portion of the assets of, or by any other manner, any business or any corporation, partnership, association or business organization or division thereof, or otherwise acquire or agree to acquire any material amount of assets other than in the ordinary course of business; *provided, however,* that notwithstanding the foregoing, the Company may acquire solely for cash or agree to acquire solely for cash equity interests or the business or assets of businesses that (i) are water or wastewater utilities, (ii) have a value not in excess of $5 million individually and $25 million in the aggregate (in each case, including the assumption of debt and other liabilities), and (iii) would not reasonably be expected to prevent or materially delay the receipt of the Company Required Statutory Approvals. The Company shall inform Parent reasonably in advance of taking, or permitting any of its subsidiaries to take, action relating to any such direct or indirect acquisition.

(e) *Capital Expenditures.* Except as set forth in Section 6.1(e) of the Company Disclosure Schedule or as required by law, the Company shall not, nor shall it permit any of its subsidiaries to, make aggregate capital expenditures that exceed 110% of the cumulative amount budgeted by the Company or its subsidiaries for capital expenditures as set forth in Section 6.1(e) of the Company Disclosure Schedule.

(f) *No Dispositions.* Except as set forth in Section 6.1(f) of the Company Disclosure Schedule, and other than in the ordinary course of business or consistent with past practice, the Company shall not, nor shall it permit any of its subsidiaries to, sell, lease, license, encumber or otherwise dispose of, any of its assets, other than encumbrances or dispositions in the ordinary course of its business consistent with past practice.

(g) *Indebtedness.* Except as set forth in Section 6.1(g) of the Company Disclosure Schedule, the Company shall not, nor shall it permit any of its subsidiaries to, incur or guarantee any indebtedness (including any debt borrowed or guaranteed or otherwise assumed including, without limitation, the issuance of debt securities or warrants or rights to acquire debt) or enter into any "keep well" or other agreement to maintain any financial statement condition of another person or enter into any arrangement having the economic effect of any of the foregoing other than (i) a net increase in short-term indebtedness in the ordinary course of business consistent with past practice in amounts not exceeding $65 million; (ii) arrangements between the Company and its wholly-owned subsidiaries or among its wholly-owned subsidiaries; (iii) net increase in total indebtedness in an amount not to exceed in the aggregate $35 million; or (iv) indebtedness in connection with acquisitions permitted by *Section 6.1(d)* hereof or long-term indebtedness in connection with the refunding of existing indebtedness either at its stated maturity or at a lower cost of funds.

(h) *Compensation, Benefits.* Except as set forth in Section 6.1(h) of the Company Disclosure Schedule, as may be required by applicable law, as may be required to facilitate or obtain a determination from the IRS that a plan is "qualified" within the meaning of Section 401(a) of the Code or as contemplated by this Agreement, the Company shall not, nor shall it permit any of its subsidiaries to, (i) enter into, adopt or amend or increase the amount or accelerate the payment or vesting of any benefit or amount payable under, any employee benefit plan or other contract, agreement, commitment, arrangement, plan or policy covering employees, former employees, directors or former directors or their beneficiaries or providing benefits to such persons that is maintained by, contributed to or entered into by such party or any of its subsidiaries, or increase or enter into any contract, agreement commitment or arrangement to increase in any manner, the compensation or fringe benefits, or otherwise to extend expand or enhance the engagement employment or any related rights of, or take any other action or grant any benefit (including, without limitation, any stock options or stock option plan) not required under the terms of any existing employee benefit plan or other contract, agreement, commitment, arrangement, plan or policy to or with any current or former director, officer or other employee of such party or any of its subsidiaries, except for normal increases or grants or actions in the ordinary course of business consistent with past practice that, in the aggregate, do not result in a material increase in benefits or compensation expense to the Company or any of its subsidiaries or (ii) enter into or amend any employment, severance or special pay arrangement with respect to the termination of employment or other similar contract, agreement or arrangement with any current or former director or officer or other employee other than in the ordinary course of business consistent with current industry practice.

(i) *Accounting.* Except as set forth in Section 6.1(i) of the Company Disclosure Schedule, the Company shall not, nor shall it permit any of its subsidiaries to, make any changes in their accounting methods, policies or procedures, except as required by law, rule, regulation or GAAP, nor shall the Company or any of its subsidiaries file any Tax Return inconsistent with past practice, or, on any such Tax Return, take any position or method that is inconsistent with positions taken, elections made or methods used in preparing or filing similar Tax Returns in prior periods, or settle or compromise any Tax liability that is subject to an audit, claim for delinquent Taxes, examination, suit or proceeding.

(j) *Cooperation, Notification.* The Company shall, and shall cause its subsidiaries to, (i) confer on a regular and frequent basis with one or more representatives of Parent to discuss, subject to applicable law, material operational matters and the general status of its ongoing operations and other matters relating to the Merger; (ii) promptly notify Parent of any significant changes in its business, properties, assets, condition (financial or other), results of operations or prospects or of the receipt of any written complaint or notice of the commencement of any investigation or proceeding which alleges the occurrence of any event or the existence of any fact which is reasonably likely to result in a Company Material Adverse Effect or the institution or, to the actual knowledge of the Company, threat of any material litigation; (iii) advise Parent of any change or event which has had or, insofar as reasonably can be foreseen, is reasonably likely to result in a Company Material Adverse Effect; and (iv) promptly provide Parent with copies of all filings made by the Company or any of its subsidiaries with any state or federal court, administrative agency, commission or other Governmental Authority in connection with this Agreement and the transactions contemplated hereby.

(k) *Third-Party Consents.* The Company shall, and shall cause its subsidiaries to, use all commercially reasonable efforts to obtain all the Company Required Consents. The Company shall promptly notify Parent of any failure or prospective failure to obtain any such consents and, if requested by Parent shall provide copies of all the Company Required Consents obtained by the Company to Parent.

(l) *No Breach, Etc.* The Company shall not, nor shall it permit any of its subsidiaries to, willfully take any action that would or is reasonably likely to result in a material breach of any provision of this Agreement or in any of its representations and warranties set forth in this Agreement being untrue on and as of the Closing Date.

(m) *Discharge of Liabilities.* The Company shall not, nor shall it permit any of its subsidiaries to, pay, discharge or satisfy any material claims, liabilities or obligations (absolute accrued, asserted or unasserted contingent or otherwise), or settle any material claim or litigation, other than the payment, discharge, satisfaction or settlement, in the ordinary course of business consistent with past practice (which includes the payment of final and non-appealable judgments) or in accordance with their terms, of liabilities reflected or reserved against in, or contemplated by, the most recent consolidated financial statements (or the notes thereto) of the Company included in the Company SEC Reports or incurred in the ordinary course of business consistent with past practice.

(n) *Contracts.* The Company shall not, nor shall it permit any of its subsidiaries to, except in the ordinary course of business consistent with past practice, modify, amend, terminate, renew or fail to use reasonable business efforts to renew any material contract or agreement to which the Company or any subsidiary of the Company is a party, or, except in connection with an acquisition permitted under *Section 6.1(d)* hereof, enter into any new material contract, or waive, release or assign any material rights or claims, or enter into any material contracts or arrangements other than on terms that are arm's length.

(o) *Insurance.* The Company shall, and shall cause its subsidiaries to, maintain with financially responsible insurance companies insurance in such amounts and against such risks and losses as are customary for companies engaged in the water utility industry.

(p) *Permits.* The Company shall, and shall cause its subsidiaries to, use reasonable efforts to maintain in effect all existing governmental permits pursuant to which such party or its subsidiaries operate.

(q) *Charter Amendments.* The Company shall not, nor shall it permit any of its subsidiaries to, amend or otherwise change its certificate of incorporation or bylaws or equivalent organizational documents or take or fail to take any other action, which in any case would reasonably be expected to prevent or materially impede or interfere with the Merger (except as permitted in *Section 6.2*).

(r) *Tax Elections.* Except as set forth in Section 6.1(r) of the Company Disclosure Schedule, the Company shall not nor shall it permit any of its subsidiaries to make, change or rescind any material Tax election, other than (i) recurring elections that customarily are made in connection with the filing of any Tax Return; provided that any such elections are consistent with the past practices of the Company or its subsidiaries, as the case may be; (ii) gain recognition agreements under Section 367 of the Code and Treasury regulations thereunder with respect to transactions occurring in the 1998 fiscal year of the Company; (iii) elections with respect to subsidiaries purchased by the Company under Section 338(h)(10) of the Code or, solely in the case of non-U.S. subsidiaries purchased by the Company, Section 338(g) of the Code; and (iv) elections with respect to partnership interests purchased by the Company under Section 754 of the Code, or settle or compromise any material Tax liability that is the subject of an audit, claim for delinquent Taxes, examination, action, suit, proceeding or investigation by any taxing authority.

(s) *Non-Competition Agreements.* Except as set forth in Section 6.1(s) of the Company Disclosure Schedule, the Company shall not nor shall it permit any of its subsidiaries to enter into any agreement, understanding or commitment that restrains, limits or impedes the Company's or any of its subsidiaries' ability to compete with or conduct any business or line of business, including, but not limited to, geographic limitations on the Company's or any of its subsidiaries' activities, other than in the ordinary course of business consistent with past practice.

(t) *Regulatory Matters.* The Company shall, and shall cause its subsidiaries to (i) timely file, in the ordinary course of business consistent with past practice, rate applications and other required filings with state public utility control or public service commissions and similar state regulatory bodies and (ii) except with respect to filings in the ordinary course of business consistent with past practice that would not reasonably be likely to have, individually or in the aggregate, a Company Material Adverse Effect, consult with Parent reasonably in advance of making any filing to implement changes in any of its or its subsidiaries' rates or surcharges for water service, standards of service or accounting or executing any agreement with respect thereto that is otherwise permitted under this Agreement. The Company shall, and shall cause its subsidiaries to, deliver to Parent a copy of each such filing or agreement.

(u) *Other Agreements.* The Company shall not nor shall it permit any of its subsidiaries to agree or enter into, in writing or otherwise, or amend any written contract or agreement that would be in violation of the covenants set forth in this *Section 6.1*.

(v) *Company Joint Ventures.* The Company shall use reasonable efforts to cause the Company Joint Ventures to operate their respective businesses only in the ordinary course consistent with past practice and, except as contemplated by *Section 7.14*, not to expand the scope of their respective businesses.

SECTION 6.2 *Alternative Proposal.*

(a) The Company shall, and shall direct and use reasonable efforts to cause its subsidiaries and any of its or its subsidiaries' directors, officers, employees, investment bankers, attorneys or other agents or representatives immediately to cease any discussions or negotiations with any parties that may be ongoing with respect to any Alternative Proposal (as defined below). The Company agrees that, prior to the Effective Time, it shall not, and shall not authorize or permit any of its subsidiaries or any of its or its subsidiaries' directors, officers, employees, investment bankers, attorneys or other agents or representatives, (x) directly or indirectly, to initiate, solicit or encourage, or take any action to facilitate the making of any offer or proposal that constitutes or is reasonably likely to lead to any Alternative Proposal or (y) directly or indirectly, engage in negotiations or provide any confidential information or data to any person relating to any Alternative Proposal. The Company shall notify Parent orally and in writing of any such inquiries, offers or proposals (including, without limitation, the terms and conditions of any such proposal). Notwithstanding anything in this *Section 6.2* to the contrary, in response to an unsolicited Alternative Proposal which did not result from a breach of this Section 6.2, unless the Company Shareholders Approval has been obtained, the Company may furnish information to, and afford access to the properties, books and records of the Company and its subsidiaries to the person making the Alternative Proposal (i) not earlier than 24 hours after providing written notice to Parent regarding such Alternative Proposal, including the terms and conditions thereof, and the identity of the person or group making the Alternative Proposal and (ii) participate in discussions with such person or group regarding the Alternative Proposal if, but only to the extent that (A) the Board of Directors of the Company has reasonably concluded in good faith (after consultation with its financial advisors) that the person or group making the Alternative Proposal will have adequate sources of financing to consummate the Alternative Proposal and that the Alternative Proposal is more favorable to the Company's shareholders than the Merger (taking into account, without limitation, the likelihood that all required regulatory approvals for such Alternative Proposal will be obtained in a prompt and timely manner), (B) the Board of Directors of the Company has determined in good faith, based on advice of outside counsel with respect to such Board's fiduciary duties under applicable law with respect to the proposed Alternative Proposal and such other matters as such Board deems relevant, that it is necessary to do so in order to act in a manner consistent with its fiduciary duties to its shareholders, and (C) such person or group has entered into a confidentiality agreement with the person or group making the Alternative Proposal (the "*Alternative Proposal Confidentiality Agreement*") containing terms and conditions no less favorable to the Company than the Confidentiality Agreement (as defined in *Section 7.1*) and the other agreements and arrangements governing the Company's relationship with Parent, it being understood that nothing herein to the contrary shall restrict the Board of Directors of the Company from exercising its authority under the Alternative Proposal Confidentiality Agreement as it may deem appropriate and (iii) not terminate this Agreement in respect of an Alternative Proposal except as provided in Section 9.1(h). The Company will keep Parent informed on a timely and current basis on the status and details (including amendments or proposed amendments) of any request for information or Alternative Proposal. The Company will immediately provide to Parent any non-public information concerning the Company provided to any other person in connection with an Alternative Proposal which was not previously provided to Parent. As used in this Agreement, "Alternative Proposal" shall mean any inquiry, proposal or offer from any person relating to any direct or indirect acquisition or purchase of a business that constitutes 20% or more of the net revenues, net income or the assets of the Company and its subsidiaries, taken as a whole, or 20% or more of any class of equity securities of the Company, or any merger, consolidation, business combination, recapitalization, liquidation, dissolution or similar transaction involving the Company, other than the transactions contemplated by this Agreement.

(b) The Board of Directors of the Company shall not withdraw or modify, or propose to withdraw or modify, in any manner adverse to Parent or Merger Sub or both, the approval or recommendation of the Board of Directors of the Company of this Agreement unless the Board of Directors of the Company shall have (i) determined in good faith as a result of changed circumstances and based on the advice of outside counsel with respect to the Board of Directors of the Company's fiduciary duties under applicable law that such fiduciary duties require the directors to withdraw or modify such approval or recommendation, and

(ii) provided to Parent a statement in writing in reasonable detail stating the reasons therefor. Notwithstanding the foregoing, nothing contained in this *Section 6.2(b)* shall prohibit the Company from taking and disclosing to stockholders a position contemplated by Rule 14e-2(a) promulgated under the Exchange Act or from making any disclosure to the Company's stockholders if, in the good faith judgment of the Board of Directors of the Company, after consultation without outside counsel, failure to so disclose would be inconsistent with its obligations under applicable law.

SECTION 6.3 ***Covenants of Parent.*** After the date hereof and prior to the Effective Time or earlier termination of their Agreement, Parent agrees, as to itself and to its subsidiaries, as follows, except as expressly contemplated or permitted in this Agreement, or to the extent the other parties hereto shall otherwise consent in writing:

(a) *Third-Party Consents.* Parent shall, and shall cause its subsidiaries to, use all commercially reasonable efforts to obtain all Parent Required Consents. Parent shall promptly notify the Company of any failure or prospective failure to obtain any such consents and, if requested by the Company, shall provide copies of all Parent Required Consents obtained by Parent to the Company.

(b) *No Breach, Etc.* Parent shall not, nor shall it permit any of its subsidiaries to, willfully take any action that would or is reasonably likely to result in a material breach of any provision of this Agreement or in any of its representations and warranties set forth in this Agreement being untrue on and as of the Closing Date.

ARTICLE VII

ADDITIONAL AGREEMENTS

SECTION 7.1 ***Access to Information.*** Upon reasonable notice and during normal business hours the Company shall, and shall cause its subsidiaries and shall use reasonable efforts to cause the Company Joint Ventures to, afford to the officers, directors, employees, accountants, counsel, investment bankers, financial advisors and other representatives of Parent (collectively, "***Representatives***") reasonable access, during normal business hours throughout the period prior to the Effective Time, to all of its properties, books, contracts, commitments and records (including, but not limited to, Tax Returns) and, during such period, the Company shall, and shall cause its subsidiaries to, furnish promptly to Parent (i) access to each report, schedule and other document filed or received by it or any of its subsidiaries pursuant to the requirements of federal or state securities laws or filed with or sent to the SEC, the Department of Justice, the Federal Trade Commission, and any other Governmental Authority, and (ii) access to all information concerning the Company, its subsidiaries, directors, officers and stockholders and such other matters as may be reasonably requested by Parent, including in connection with any filings, applications or approvals required or contemplated by this Agreement; *provided* that no investigation pursuant to this *Section 7.1* shall affect any representation or warranty made herein or any condition to the obligations of the respective parties to consummate the Merger. Parent shall, in accordance with the Confidentiality Agreement dated as of July 26, 1999 between the Company and Parent (the "Confidentiality Agreement"), and shall cause its subsidiaries and Representatives to, hold in strict confidence all information concerning the Company furnished to it in connection with the transactions contemplated by this Agreement.

SECTION 7.2 ***Proxy Statement.***

(a) The Company will prepare and file the Proxy Statement with the SEC as soon as reasonably practicable after the date hereof and shall use all reasonable efforts to have the Proxy Statement cleared by the SEC at the earliest practicable time. Parent, Merger Sub and the Company shall cooperate with each other in the preparation of the Proxy Statement, and the Company shall notify Parent of the receipt of any comments of the SEC with respect to the Proxy Statement and of any requests by the SEC for any amendment or supplement thereto or for additional information and shall provide to Parent promptly copies of all correspondence between the Company, or any representative of the Company, and the SEC or its staff. The Company shall give Parent and their counsel the opportunity to review the Proxy Statement prior to its being filed with the SEC and shall give Parent and their counsel the opportunity to review all amendments and supplements to the Proxy Statement and all responses to requests for additional information and replies to comments prior to their being filed with, or sent to, the SEC. Each of the Company, Parent and Merger Sub agrees to use all reasonable efforts, after consultation with the other parties hereto, to respond promptly to all such comments of and requests by the SEC and to cause the Proxy Statement and all required amendments and supplements thereto to be mailed to the holders of Shares entitled to vote at the Company Special Meeting at the earliest practicable time. Parent shall furnish all information concerning itself which is required or customary for inclusion in such Proxy Statement. The information provided by Parent for use in the Proxy Statement shall be true and correct in all material respects without omission of any material fact which is required to make such information not false or misleading. No representation, covenant or agreement is made by or on behalf of the Company with respect to information supplied by Parent for inclusion in the Proxy Statement.

(b) If, at any time prior to the Effective Time, any event with respect to the Company, its officers and directors or any of its subsidiaries should occur which is required to be described in an amendment of, or a supplement to, the Proxy Statement, such event shall be so described, and such amendment or supplement shall be promptly filed with the SEC and, as required by law, disseminated to the Company's stockholders. Prior to the filing of such amendment or supplement with the SEC, a copy thereof will be delivered to Parent and their counsel, who shall, to the extent practicable under the circumstances and applicable law, have the opportunity to comment on such amendment or supplement.

SECTION 7.3 ***Regulatory Matters.*** Each party hereto shall cooperate and use its best efforts to promptly prepare and file all necessary documentation to effect all necessary applications, notices, petitions, filings and other documents, and to use all commercially reasonable efforts to obtain as soon as reasonably practicable following the date hereof all necessary permits, consents, approvals and authorizations of all Governmental Authorities necessary or advisable to consummate the transactions contemplated by this Agreement, including, but not limited to, (a) all notifications required to be filed under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, and the rules and regulations thereunder, (b) the other Company Required Statutory Approvals and (c) the other Parent Required Statutory Approvals. The parties agree that they will consult with each other with respect to obtaining Company Required Statutory Approvals and the Parent Required Statutory Approvals; provided, however, that it is agreed that the Company shall have primary responsibility for the preparation and filing of any applications, filings or other material with state utility commissions required to be filed or submitted in connection with obtaining the Company Required Statutory Approvals. Parent shall have the right to review and approve in advance drafts of and final applications, filings and other material submitted to or filed with state utility commissions, which approval shall not be unreasonably conditioned, withheld or delayed.

SECTION 7.4 *Stockholder Approval.*

(a) *The Company Stockholders.* Subject to the provisions of *Section 7.4(b)* and the NJBCA, the Company shall, as soon as reasonably practicable after the date hereof (i) take all steps necessary to duly call, give notice of, convene and hold a meeting of its stockholders (the "*Company Special Meeting*") for the purpose of securing Company Stockholders' Approval, (ii) distribute to its stockholders the Proxy Statement in accordance with applicable federal and state law and with its certificate of incorporation and by-laws, (iii) subject to *Section 6.2(b)*, recommend to its stockholders the approval of this Agreement and the transactions contemplated hereby, (iv) subject to *Section 6.2(b)*, use its reasonable best efforts to obtain the Company Stockholders' Approval at the Company Special Meeting, and (v) cooperate and consult with Parent with respect to each of the foregoing matters.

(b) *Meeting Date.* Subject to *Section 7.4(a)*, the Company Special Meeting for the purpose of securing the Company Stockholders' Approval shall be held on such date as the Company shall determine.

SECTION 7.5 ***Directors' and Officers' Indemnification.***

(a) *Indemnification.* To the extent, if any, not provided by an existing right of indemnification or other agreement or policy, after the Effective Time, Parent, the Surviving Corporation and the Company shall, to the fullest extent permitted by applicable law, indemnify, defend and hold harmless each person who is now, or has been at any time prior to the date hereof, or who becomes prior to the Effective Time, an officer or director of any of the parties hereto or any subsidiary (each, an ''*Indemnified Party*'' and collectively, the ''*Indemnified Parties*'') against (i) all losses, expenses (including reasonable attorneys' fees and expenses), claims, damages or liabilities or, subject to the proviso of the next sentence, amounts paid in settlement, arising out of actions or omissions occurring at or prior to the Effective Time (and whether asserted or claimed prior to, at or after the Effective Time) that are, in whole or in part, based on or arising out of the fact that such person is or was a director or officer of such party or a subsidiary of such party (the ''*Indemnified Liabilities*''), and (ii) all Indemnified Liabilities to the extent they are based on or arise out of or pertain to the transactions contemplated by this Agreement. In the event of any such loss, expense, claim, damage or liability (whether or not arising before the Effective Time), (i) Parent shall pay the reasonable fees and expenses of counsel selected by the Indemnified Parties, which counsel shall be reasonably satisfactory to Parent, promptly after statements therefor are received and otherwise advance to such Indemnified Party upon request reimbursement of documented expenses reasonably incurred, (ii) Parent and the Company will cooperate in the defense of any such matter and (iii) any determination required to be made with respect to whether an Indemnified Party's conduct complies with the standards set forth under New Jersey law and other applicable law, and the certificate of incorporation or by-laws shall be made by independent counsel mutually acceptable to Parent and the Indemnified Party; *provided, however*, that Parent shall not be liable for any settlement effected without its written consent (which consent shall not be unreasonably withheld). The Indemnified Parties as a group may retain only one law firm with respect to each related matter except to the extent there is, in the written opinion of counsel to an Indemnified Party, under applicable standards of professional conduct, a conflict on any significant issue between positions of such Indemnified Party and any other Indemnified Party or Indemnified Parties. Any Indemnified Party wishing to claim indemnification under this *Section 7.5*, upon learning of any such claim, action, suit or proceeding eligible for indemnification under this *Section 7.5*, shall notify the Indemnifying Parties, but the failure so to notify an Indemnifying Party shall not relieve it from any liability which it may have under this *Section 7.5*, except to the extent that such failure results in the forfeiture of substantive rights or defenses.

(b) *Insurance.* For a period of six years after the Effective Time, Parent shall cause to be maintained in effect policies of directors' and officers' liability insurance for the benefit of those persons who are currently covered by such policies of the Company or its Subsidiaries on terms no less favorable than the terms of such current insurance coverage; *provided, however*, that Parent shall not be required to expend in any year an amount in excess of two hundred percent (200%) of the annual aggregate premiums currently paid by the Company, for such insurance; and *provided, further*, that if the annual premiums of such insurance coverage exceed such amount, Parent shall be obligated to obtain a policy with the best coverage available, in the reasonable judgment of the Board of Directors of Parent, for a cost not exceeding such amount.

(c) *Successors.* In the event Parent or any of its successors or assigns (i) consolidates with or merges into any other person and shall not be the continuing or surviving corporation or entity of such consolidation or merger or (ii) transfers all or substantially all of its properties and assets, then and in either such case, proper provisions shall be made so that the successors and assigns of Parent shall assume the obligations set forth in this *Section 7.5*.

(d) *Survival of Indemnification.* To the fullest extent permitted by law, from and after the Effective Time, all rights to indemnification as of the date hereof in favor of the directors and officers of the Company, and its subsidiaries with respect to their activities as such prior to the Effective Time, as provided in its respective certificate of incorporation and by-laws in effect on the date hereof, or otherwise in effect on the date hereof, shall survive the Merger and shall continue in full force and effect for a period of not less than six years from the Effective Time.

(e) *Benefit.* The provisions of this *Section 7.5* are intended to be for the benefit of, and shall be enforceable by, each Indemnified Party, his or her heirs and his or her representatives.

SECTION 7.6 ***Disclosure Schedules.*** On the date hereof, (i) Parent has delivered to the Company a schedule (the "*Parent Disclosure Schedule*"), accompanied by a certificate signed by the chief financial officer of Parent stating the Parent Disclosure Schedule is being delivered pursuant to this *Section 7.6(i)* and *(ii)* the Company has delivered to Parent a schedule (the "*Company Disclosure Schedule*"), accompanied by a certificate signed by the chief financial officer of the Company stating the Company Disclosure Schedule is being delivered pursuant to this *Section 7.6(ii)*. The Company Disclosure Schedule and the Parent Disclosure Schedule are collectively referred to herein as the "*Disclosure Schedules*". The Disclosure Schedules constitute an integral part of this Agreement and modify the respective representations, warranties, covenants or agreements of the parties hereto contained herein to the extent that such representations, warranties, covenants or agreements expressly refer to the Disclosure Schedules. Anything to the contrary contained herein or in the Disclosure Schedules notwithstanding, any and all statements, representations, warranties or disclosures set forth in the Disclosure Schedules shall be deemed to have been made on and as of the date hereof.

SECTION 7.7 ***Public Announcements.*** Subject to each party's disclosure obligations imposed by law, the Company and Parent will cooperate with each other in the development and distribution of all news releases and other public information disclosures with respect to this Agreement or any of the transactions contemplated hereby and, except as may be required by law or the rules of any applicable stock exchange, shall not issue any public announcement or statement with respect hereto without the consent of the other party (which consent shall not be unreasonably withheld).

SECTION 7.8 ***Certain Employee Agreements.*** Subject to *Section 7.9*, Parent and the Company and its subsidiaries shall honor, without modification, all contracts, agreements, collective bargaining agreements and commitments of the parties prior to the date hereof which apply to any current or former employee or current or former director of the parties hereto; *provided, however*, that this undertaking is not intended to prevent Parent or the Company from enforcing or complying with such contracts, agreements, collective bargaining agreements and commitments in accordance with their terms, including, without limitation, exercising any right to amend, modify, suspend, revoke or terminate any such contract, agreement, collective bargaining agreement or commitment under any such contract, agreement, collective bargaining agreement or commitment or under applicable law. Any workforce reductions carried out following the Effective Time by Parent or the Company and their subsidiaries shall be done in accordance with all applicable collective bargaining agreements, and all laws and regulations governing the employment relationship and termination thereof, including, without limitation, the Worker Adjustment and Retraining Notification Act and regulations promulgated thereunder, and any comparable state or local law.

SECTION 7.9 ***Employee Benefit Plans.***

(a) *Maintenance of the Company Benefit Plans.* Each of the Company Benefit Plans (other than Company Stock Plans) in effect at the date hereof shall be maintained in effect with respect to the employees or former employees of the Company and any of its subsidiaries, who are covered by any such benefit plan immediately prior to the Closing Date (the "*Affiliated Employees*") until Parent or the Company otherwise determine after the Effective Time; *provided, however*, that nothing herein contained shall limit any right contained in any such Company Benefit Plan or under applicable law to amend, modify, suspend, revoke or terminate any such plan; *provided further, however*, that Parent or the Company or their subsidiaries shall provide benefits to the Affiliated Employees for a period of not less than one year following the Effective Time which are no less favorable in the aggregate than those provided under the Company Benefit Plans (with respect to employees and former employees of the Company and its subsidiaries). Without limitation of the foregoing, each participant in any such Company Benefit Plan shall receive credit for purposes of eligibility to participate, vesting, and eligibility to receive benefits under any benefit plan of the Company or any of its subsidiaries or affiliates for service credited for the corresponding purpose under such benefit plan; *provided, however*, that such crediting of service shall not operate to duplicate any benefit to any such participant or the funding for any such benefit or cause any such Company Benefit Plan to fail to comply with the applicable provisions of the Code or ERISA.

(b) *Welfare Benefits Plans.* With respect to any welfare benefit plan established to replace any Company Benefit Plan which is a welfare benefit plan in which Affiliated Employees may be eligible to participate after the Closing Date, other than limitations, exclusions or waiting periods that are already in effect with respect to such Affiliated Employees and that have not been satisfied as of the Closing Date, such replacement plans shall waive all limitations to pre-existing conditions, exclusions and waiting periods with respect to participation and coverage requirements and provide each Affiliated Employee with credit for other co-payments and deductibles paid prior to the Closing Date in satisfying any applicable deductible or out-of-pocket requirements applicable to the same calendar year under any welfare plans that such Affiliated Employees are eligible to participate in after the Closing Date.

SECTION 7.10 ***The Company Stock Plans.*** With respect to each Company Benefit Plan or other plan, agreement or arrangement that provides for benefits in the form of Company Common Stock or options to purchase Company Common Stock (the "*Company Stock Plans*"), the Company and its subsidiaries and Parent and its subsidiaries, including the Surviving Corporation and its subsidiaries, shall take all actions necessary to provide that upon the Effective Time, (i) each outstanding option to purchase Company Common Stock under any Company Stock Plan, whether or not then vested and exercisable, shall be canceled in exchange for a cash payment equal to (A) the excess of the Per Share Cash Consideration over the exercise price thereof times (B) the number of shares of Company Common Stock subject thereto, less applicable tax withholding, and (ii) each outstanding restricted share of Company Common Stock granted under any Company Stock Plans shall become fully vested as provided in the applicable Company Stock Plan and shall be simultaneously converted into the right to receive the Per Share Cash Consideration as provided in *Section 2.1*. The Company and its subsidiaries shall take all actions needed to terminate all Company Stock Plans, subject, however, to the payments required under the preceding sentence.

SECTION 7.11 ***Expenses.*** Subject to *Section 9.3*, all costs, and expenses incurred in connection with this Agreement and the transactions contemplated hereby shall be paid by the party incurring such expenses.

SECTION 7.12 ***Further Assurances.*** Each party will, and will cause its subsidiaries to, (i) execute such further documents and instruments and use their reasonable best efforts to take such further actions as may be necessary or appropriate or as may reasonably be requested by any other party in order to consummate the Merger in accordance with the terms hereof, and (ii) not take action (including effecting or agreeing to effect or announcing an intention or proposal to effect any acquisition, business combination or other transaction) which could reasonably be expected to impede, interfere with, prevent, impair or delay the ability of the parties to consummate the Merger. In case at any time any further action is necessary or desirable to carry out the terms and provisions of this Agreement, the proper officers and directors of each party to this Agreement shall use their reasonable best efforts to take all such action.

SECTION 7.13 ***Governance Agreement.***

(a) *General.* Except as set forth herein, the terms and conditions of the Governance Agreement, dated as of April 22, 1994, as amended, between Parent and the Company (the "Governance Agreement") shall remain in full force and effect and the parties shall continue to be fully bound by the provisions thereof as modified hereby. The Company and Parent agree that the Governance Agreement is hereby modified (i) as expressly set forth in *Section 7.13(b)* hereof, (ii) as long as this Agreement is in effect, to waive any provisions of the Governance Agreement that are inconsistent with *Section 6.2* hereof, including the "30 day" right granted to Parent under Section 3.1(a) of the Governance Agreement and Parent's right to acquire the Company Common Stock during any "Second 120-day Period" as defined in Section 3.1(b) of the Governance Agreement, and (iii) as may otherwise be required to give effect to the provisions of this Agreement.

(b) *Waivers Upon Acceptance of Alternative Proposal.* Upon any termination of this Agreement by the Company pursuant to *Section 9.1(h)* hereof, the Company shall, and it hereby does, waive any and all obligations of or restrictions on Parent and affiliates contained in Sections 3.7 (Conversion of Preference Stock).

(c) *Waivers Upon Termination of Agreement in Certain Circumstances.* If this Agreement is terminated by the Company pursuant to *Section 9.1(h)*, by Parent pursuant to *Section 9.1(e)* or by either the Company or Parent pursuant to *Section 9.1(c)* due to the failure to obtain the approval of the Company's stockholders at the Company Special Meeting and at the time of such failure, any person shall have made a public announcement or otherwise communicated to the Company or its stockholders with respect to an Alternative Proposal with respect to the Company which has not been rejected by the Company and terminated or withdrawn by the party making the Alternative Proposal, then:

(1) Notwithstanding anything in Sections 3.1(a) or (b) or Sections 3.3(a), (d) or (e) of the Governance Agreement to the contrary, Parent shall be permitted to make a proposal or proposals to the Board of Directors of the Company for the acquisition of 100% of the outstanding equity of the Company or substantially all of the assets of the Company and its subsidiaries during the period commencing on the date of termination of this Agreement and ending on the date 120 days after such date if the Company has not entered into a definitive agreement with a third party effecting an Alternative Proposal during such 120 day period, or if the Company enters into such definitive Agreement with a third party during such 120 day period, the earlier of the date on which the Company's stockholders approve such Alternative Proposal or the date on which such definitive agreement is terminated. Parent agrees that it shall have no "30 day" right with respect to any third party Alternative Proposal made during such period.

(2) Notwithstanding anything in Sections 4.1(a) and (b) of the Governance Agreement to the contrary, Parent shall not be required to vote any Company Common Stock in favor of any Alternative Proposal; provided, however, that if Parent determines not to vote in favor of any Alternative Proposal, it shall, at the request of the Company, not be present at the shareholders meeting at which approval of the Alternative Proposal is sought for quorum or any other purposes.

SECTION 7.14 ***North American Rights Agreement.***

(a) *General.* The Company and Parent agree that, except as otherwise set forth in this *Section 7.14(b)*, the terms and conditions of the North American Rights Agreement, dated July 14, 1997, as amended, among the Company, Parent and other parties (the "*NARA*") shall remain in full force and effect and further agree, except as set forth in *Section 7.14(b)*, to continue to be fully bound by the provisions thereof.

(b) *Exceptions for Market Opportunities.* In order to permit the Company and Parent to respond appropriately to market opportunities while this Agreement is in effect, notwithstanding any contrary provisions of the NARA, Parent and the Company, on their own behalf and on behalf of their respective affiliates, agree as follows:

(i) *Acquisitions of Rate-Regulated Businesses.*

(A) *Acquisitions Prior to Termination.* From the date hereof until the termination of this Agreement, (1) the Company and its subsidiaries may acquire or invest in rate-regulated water and wastewater utility businesses as permitted by *Section 6.1(d)* hereof and (2) Parent and its affiliates may acquire or invest in rate-regulated water and wastewater utility businesses in the United States, *provided* that neither Parent nor any of its affiliates shall make or agree to make any such acquisition or investment if such acquisition or agreement could reasonably be expected to prevent, or materially delay the receipt of regulatory approvals necessary to consummate the Merger.

(B) *Rights After Termination.*

(1) *The Company's Right to Acquire Regulated Company Interests.* Subject to *Section 7.14(b)(i)(B)(2)*, from the date of termination of this Agreement through the first anniversary of such termination, the Company shall have the right and option, on not less that 15 days' notice to Parent, to purchase up to 50% of any interests in regulated water businesses in the United States acquired by Parent or its affiliates as permitted by *Section 7.14(b)(i)(A)* (each, a "*Regulated Company Interest*"). The price of any portion of a Regulated Company Interest

purchased by the Company under this subsection shall equal the full cost of the interest to be transferred, including (1) a pro rata portion of the consideration paid by Parent or such affiliate to acquire the Regulated Company Interest, (2) a pro rata portion of the actual out-of-pocket third party transaction costs (including fees and disbursements of counsel and other advisors) incurred by Parent or such affiliate in acquiring the Regulated Company Interest, and (3) interest on the foregoing amounts at the rate of 8.00% per annum from the date the Regulated Company Interest was acquired by Parent or its affiliate through the date of transfer to the Company.

(2) *Parent Right to Retain Regulated Company Interests.* If (w) the Company shall terminate this Agreement pursuant to *Section 9.1(h)*, (x) Parent shall terminate this Agreement pursuant to *Section 9.1(e)*, (y) Parent or the Company shall terminate this Agreement pursuant to *Section 9.1(c)* due to the failure to obtain the approval of the Company' stockholders at the Company Special Meeting and, at the time of such failure, any person shall have made a public announcement or otherwise communicated to the Company or its stockholders with respect to an Alternative Proposal with respect to the Company which has not been rejected by the Company and terminated or withdrawn by the party making the Alternative Proposal, or (z) Parent shall terminate this Agreement for a Terminating the Company Breach pursuant to *Section 9.1(g)*, then, notwithstanding *Section 7.14(b)(i)(B)(1)*, Parent and its affiliates shall have the right to own and retain any and all Regulated Company Interests that (x) they may have acquired prior to such termination or (y) with respect to which Parent or its affiliates shall have entered into a binding commitment or agreement prior to such termination, and, in each case, the right to manage, operate and control the business thereof.

(ii) *Acquisitions of Delegated Services Businesses.*

(A) *UWS Entity Right of First Refusal.*

(1) *Rights to Acquire Delegated Services Company Interests.* United Water Services LLC, a Delaware limited liability company ("*UWS*"), United Water Services Canada L.P., an Ontario, Canada limited partnership ("*UWS Canada*"), and United Water Services Mexico LLC, a Delaware limited liability company ("*UWS Mexico*"), each of which is owned jointly by Parent and the Company (each, a "*UWS Entity*"), shall have the right, at its sole option (each, a "*UWS Option*"), to purchase on the terms and subject to the conditions set forth in this *Section 7.14(b)(ii)* all but not less than all of any interests in Delegated Services Providers (as defined in the NARA) in the United States, Canada or Mexico, respectively (each, a "*Delegated Services Company Interest*"), that Parent or any of its affiliates wishes to acquire under this *Section 7.14(b)(ii)*. From the date hereof until the termination of this Agreement, Parent and its affiliates shall have the right to acquire any and all such Delegated Services Company Interests subject only to the UWS Option.

(2) *Exercise of UWS Option.* Prior to acquiring any Delegated Services Company Interest, Parent (or its affiliate, as the case may be) shall first give written notice to the applicable UWS Entity of such proposed acquisition (a "*Notice of Option*"). Each such Notice of Option shall include the identity of the proposed target, the terms of the proposed acquisition and the price or other consideration proposed to be paid for such Delegated Services Company Interest. The applicable UWS Entity may exercise any UWS Option by written notice to Parent given within 15 days after the date of the applicable Notice of Option. If such UWS Entity fails to exercise any UWS Option for any reason other than a Parent Veto (defined below), or if such UWS Entity fails to acquire any Delegated Services Company Interest with respect to which it has exercised a UWS Option within 90 days of such exercise, Parent (or its affiliate) shall have the right to purchase such Delegated Services Company Interest at the price and on substantially the terms set forth in the applicable Notice of Option.

(3) If the acquisition of any Delegated Services Company Interest by either a UWS Entity or Parent and/or any of its affiliates could reasonably be expected to prevent or materially delay

the receipt of regulatory approvals necessary to consummate the Merger, then, notwithstanding anything to the contrary set forth in this *Section 7.14(b)(i)*, Parent and its affiliates shall not have the right to acquire such Delegated Services Company Interest without first obtaining the prior written consent of the Company.

(4) As used in this *Section 7.14(b)(ii)*, "Parent Veto" means (1) a failure of the Board of Managers of UWS or UWS Mexico, or the Board of Directors of the general partner of UWS Canada, to approve the exercise of the UWS Option with respect to any Delegated Services Company Interest solely due to one or more Managers or Directors appointed by Parent to such Board voting against the exercise of such UWS Option or (2) a failure of the members or partners of such UWS Entity to approve the exercise of the UWS Option with respect to such Delegated Services Company Interest solely due to Parent voting against the exercise of such UWS Option, if a vote of the members or partners is required for such approval.

(B) *Rights After Termination.*

(1) Subject to *Section 7.14(b)(ii)(B)(2)*, from the date of termination of this Agreement through the first anniversary of such termination, the UWS Entities shall have the right and option, without regard to any Parent Veto, on not less than 15 days' notice to Parent, to purchase all but not less than all of any Delegated Services Company Interests acquired by Parent or any affiliate thereof in accordance with this *Section 7.14(b)*. The price of any Delegated Services Company Interest purchased by a UWS Entity under this subsection shall equal the full cost of such Delegated Services Company Interest, including (1) the consideration paid by Parent or such affiliate to acquire the Delegated Services Company Interest, (2) the actual out-of-pocket third party transaction costs (including fees and disbursements of counsel and other advisors) incurred by Parent or such affiliate in acquiring the Delegated Services Company Interest, and (3) interest on the foregoing amounts at the rate of 8% per annum from the date the Delegated Services Company Interest was acquired by Parent or its affiliate through the date of transfer to the UWS Entity.

(2) If (w) the Company shall terminate this Agreement pursuant to *Section 9.1(h)*, (x) Parent shall terminate this Agreement pursuant to *Section 9.1(e)*, (y) Parent or the Company shall terminate this Agreement pursuant to *Section 9.1(c)* due to the failure to obtain the approval of the Company's stockholders at Company Special Meeting and, at the time of such failure, any person shall have made a public announcement or otherwise communicated to the Company or its stockholders with respect to an Alternative Proposal with respect to the Company which has not been rejected by the Company and terminated or withdrawn by the party making the Alternative Proposal, or (z) Parent shall terminate this Agreement for a Terminating Company Breach pursuant to *Section 9.1(g)*, then, notwithstanding *Section 7.14(b)(ii)(B)(1)*, Parent and its affiliates shall have the right to own and retain any and all Delegated Services Company Interests that (x) they may have acquired prior to such termination or (y) with respect to which Parent or its affiliates shall have entered into a binding commitment or agreement prior to such termination, and, in each case, the right to manage, operate and control the business thereof.

SECTION 7.15 ***Notice and Cure.*** The Company will notify Parent in writing of, and will use all commercially reasonable efforts to cure before the Closing, any event, transaction or circumstance, as soon as practicable after it becomes known to the Company, that causes or will or may be likely to cause any covenant or agreement of the Company under the Agreement to be breached or that renders or will render untrue in any material respect any representation or warranty of the Company contained in the Agreement. No notice given pursuant to this paragraph shall have any effect on the representations, warranties, covenants or agreements contained in the Agreement for purposes of determining satisfaction of any condition contained in the Agreement.

ARTICLE VIII

CONDITIONS

SECTION 8.1 ***Conditions to Each Party's Obligation to Effect the Merger.*** The respective obligations of each party to effect the Merger shall be subject to the satisfaction on or prior to the Closing Date of the following conditions, except that such conditions may be waived in writing pursuant to *Section 9.5* by the joint action of the parties hereto to the extent permitted by applicable law:

(a) *Stockholder Approval.* The Company Stockholders' Approval shall have been obtained.

(b) *No Injunction.* No temporary restraining order or preliminary or permanent injunction or other order, decree, ruling or action taken by any United States or French federal or state court of competent jurisdiction or other United States or French federal or state or other governmental authority of competent jurisdiction restraining, enjoining or otherwise prohibiting the Merger shall have been issued and be continuing in effect, and the Merger and the other transactions contemplated hereby shall not have been prohibited under any United States or French federal or state or other applicable law, order, rule or regulation.

(c) *Statutory Approvals.* The Company Required Statutory Approvals and the Parent Required Statutory Approvals shall have been obtained at or prior to the Effective Time, such approvals shall have become Final Orders (as defined below) and such Final Orders shall not impose terms or conditions which, individually or in the aggregate, insofar as reasonably can be foreseen, will have, a Company Material Adverse Effect. A "*Final Order*" means action by the relevant regulatory authority which has not been reversed, stayed, enjoined, set aside, annulled or suspended, with respect to which any waiting period prescribed by law before the transactions contemplated hereby may be consummated has expired, and as to which all conditions to the consummation of such transactions prescribed by law, regulation or order have been satisfied.

SECTION 8.2 ***Conditions to Obligation of Parent to Effect the Merger.*** The obligation of Parent and Merger Sub to effect the Merger shall be further subject to the satisfaction, on or prior to the Closing Date, of the following conditions except as may be waived by Parent and Merger Sub in writing pursuant to *Section 9.5*:

(a) *Performance of Obligations of the Company.* The Company (and/or its appropriate subsidiaries) shall have performed in all material respects its agreements and covenants contained in or contemplated by this Agreement to be performed by it at or prior to the Effective Time.

(b) *Representations and Warranties.* The representations and warranties of the Company set forth in this Agreement shall be true and correct in all material respects (i) on and as of the date hereof and (ii) on and as of the Closing Date with the same effect as if such representations and warranties had been made on and as of the Closing Date (other than representations and warranties that expressly speak only as of a specific date or time other than the date hereof or the Closing Date which need only be true and correct as of such date or time) except, in the case of representations and warranties other than those contained in *Section 4.2* (but only to the extent that such Section contains a representation as to the ownership of the Company of its subsidiaries described in clause (x) of the first sentence thereof) and *Sections 4.3(a)*, *4.4(a)*, *4.15* and *4.16*, for such failures of representations and warranties to be true and correct (determined without regard to any materiality standard contained therein) which individually or in the aggregate would not be reasonably likely to result in a Company Material Adverse Effect.

(c) *Closing Certificates.* Parent shall have received a certificate signed by the chief financial officer of the Company, dated the Closing Date, to the effect that, to the best of such officer's knowledge, the conditions set forth in *Section 8.2(a)* and *Section 8.2(b)* have been satisfied.

(d) *No Company Material Adverse Effect.* No Company Material Adverse Effect shall have occurred and be continuing and there shall exist no fact or circumstance which individually or in the aggregate would reasonably be likely to have a Company Material Adverse Effect.

(e) *Company Required Consents.* Company Required Consents the failure of which to obtain would, individually or in the aggregate, reasonably be likely to have a Company Material Adverse Effect shall have been obtained.

(f) *Other Evidence.* Parent and Merger Sub shall have received from the Company such further certificates and documents evidencing due action in accordance with this Agreement, including certified copies of proceedings of the Board of Directors and stockholders of the Company, as Parent or Merger Sub reasonably shall request.

SECTION 8.3 ***Conditions to Obligation of the Company to Effect the Merger.*** The obligation of the Company to effect the Merger shall be further subject to the satisfaction, on or prior to the Closing Date, of the following conditions, except as may be waived by the Company in writing pursuant to *Section 9.5*.

(a) *Performance of Obligations of Parent.* Parent (and/or its appropriate subsidiaries) shall have performed in all material respects its agreements and covenants contained in or contemplated by this Agreement to be performed by it at or prior to the Effective Time.

(b) *Representations and Warranties.* The representations and warranties of Parent set forth in this Agreement shall be true and correct in all material respects (i) on and as of the date hereof and (ii) on and as of the Closing Date with the same effect as though such representations and warranties had been made on and as of the Closing Date (other than representations and warranties that expressly speak only as of a specific date or time other than the date hereof or the Closing Date which need only be true and correct as of such date or time) except for such failures of representations and warranties to be true and correct (determined without regard to any materiality standard) which individually or in the aggregate would not be reasonably likely to result in a Parent Material Adverse Effect.

(c) *Closing Certificates.* The Company shall have received a certificate signed by the chief financial officer of Parent, dated the Closing Date to the effect that, to the best of such officer's knowledge, the conditions set forth in *Section 8.3(a)* and *Section 8.3(b)* have been satisfied.

ARTICLE IX

TERMINATION, AMENDMENT AND WAIVER

SECTION 9.1 ***Termination.*** This Agreement may be terminated at any time prior to the Closing Date, whether before or after approval by the stockholders of the respective parties hereto contemplated by this Agreement:

(a) by mutual written consent of the Boards of Directors of the Company and Parent;

(b) by either Parent or the Company, by written notice to the other party, if the Effective Time shall not have occurred on or before the twelve month anniversary of the date hereof (the "*Initial Termination Date*"); *provided, however*, that the right to terminate the Agreement under this *Section 9.1(b)* shall not be available to any party whose failure to fulfill any obligation under this Agreement has been the cause of, or resulted in, the failure of the Effective Time to occur on or before such date; and *provided, further*, that if on the Initial Termination Date the conditions to the Closing set forth in *Sections 8.1(c)* and/or *8.2(e)* shall not have been fulfilled but all other conditions to the Closing shall be fulfilled or shall be capable of being fulfilled, then the Initial Termination Date shall be extended to the eighteen month anniversary of the date hereof;

(c) by either Parent or the Company, by written notice to the other party if the Company Stockholders' Approval shall not have been obtained at a duly held Company Special Meeting, including any adjournments thereof;

(d) by either Parent or the Company, if any United States or French federal, state or other law, order, rule or regulation is adopted or issued, which has the effect, as supported by the written opinion of outside counsel for such party, of prohibiting the Merger, or by any party hereto if any United States or French federal, state or other court of competent jurisdiction or other United States federal or state or French governmental authority of competent jurisdiction shall have issued an order, decree or ruling, or taken any other action, restraining, enjoining or otherwise prohibiting the Merger, and such order, decree or ruling or other action shall have become final and non-appealable;

(e) by Parent, if (i) the Board of Directors of the Company withdraws, modifies or changes its approval or recommendation of this Agreement in a manner adverse to Parent or shall have resolved to do so, (ii) the Board of Directors of the Company shall have recommended to the stockholders of the Company an Alternative Proposal or shall have resolved to do so, or (iii) a tender offer or exchange offer for 20% or more of the outstanding shares of capital stock of the Company is commenced and the Board of Directors of the Company fails to recommend against acceptance of such tender offer or exchange offer by its stockholders (including by taking no position with respect to the acceptance of such tender offer or exchange offer by its stockholders);

(f) by the Company, by written notice to Parent, if (i) there exist breaches of the representations and warranties of Parent made herein as of the date hereof which breaches, individually or in the aggregate, would or would be reasonably likely to result in a Parent Material Adverse Effect, and such breaches shall not have been remedied within 20 days after receipt by Parent of notice in writing from the Company, specifying the nature of such breaches and requesting that they be remedied, or (ii) Parent (and/or its appropriate subsidiaries) shall not have performed and complied with, in all material respects, its agreements and covenants hereunder and such failure to perform or comply shall not have been remedied within 20 days after receipt by Parent of notice in writing from the Company, specifying the nature of such failure and requesting that it be remedied;

(g) by Parent, by written notice to the Company, if (i) there exist material breaches of the representations and warranties of the Company made herein as of the date hereof which breaches, individually or in the aggregate, would or would be reasonably likely to result in a Company Material Adverse Effect, and such breaches shall not have been remedied within 20 days after receipt by the Company of notice in writing from Parent, specifying the nature of such breaches and requesting that they be remedied, (ii) the Company (and/or its appropriate subsidiaries) shall not have performed and complied with its agreements and covenants contained in *Sections 6.1(b)* and *6.1(c)* or shall have failed to perform and comply with, in all material respects, its other agreements and covenants hereunder, and such failure to perform or comply shall not have been remedied within 20 days after receipt by the Company;

(h) prior to the Company Shareholders' Approval, by the Company, upon five (5) Business Days' prior written notice to Parent, if, as a result of any written offer or proposal in respect of an Alternative Proposal, the Board of Directors of the Company determines that such written offer or proposal be accepted; *provided, however*, that (i)(A) the Board of Directors of the Company shall have reasonably concluded in good faith (after consultation with its financial advisors) that the person or group making the Alternative Proposal will have adequate sources of financing to consummate the Alternative Proposal and that the Alternative Proposal is more favorable to the Company shareholders than the Merger (taking into account, without limitation, the likelihood that all required regulatory approvals for such Alternative Proposal will be obtained in a prompt and timely manner) and (B) the Board of Directors of the Company shall have determined in good faith, based on advice of outside counsel with respect to such Board's fiduciary duties under applicable law with respect to the proposed Alternative Proposal as the Board of Directors deem to be relevant, that, notwithstanding a binding commitment to consummate an agreement of the nature of this Agreement entered into in the proper exercise of their applicable fiduciary duties, and notwithstanding all modifications that may be offered by Parent in negotiations entered into pursuant to clause (ii) below, such fiduciary duties would also require the directors to reconsider such commitment and terminate this Agreement as a result of such written offer or proposal and (ii) prior to any such termination, the Company shall, and shall cause its respective financial and legal advisors to, negotiate in good faith with Parent to make such adjustments in the terms and conditions of this Agreement as would not require termination of this Agreement.

SECTION 9.2 ***Effect of Termination.*** In the event of termination of this Agreement pursuant to Section 9.1 there shall be no liability under this Agreement on the part of Parent, Merger Sub or the Company or any of their respective representatives, and all rights and obligations of each party hereto shall cease, except as set forth in *Sections 6.2, 7.14, 9.3* and *10.1*; *provided, however*, that nothing in this Agreement shall relieve any party from liability for the willful breach of any of its representations and warranties or the breach of any of its covenants or agreements set forth in this Agreement.

SECTION 9.3 ***Termination Fee; Expenses.***

(a) The Company agrees that, if (i) the Company shall terminate this Agreement pursuant to *Section 9.1(h)*, (ii) Parent shall terminate this Agreement pursuant to *Section 9.1(e)*, or (iii) Parent or the Company shall terminate this Agreement pursuant to Section 9.1(c) due to the failure to obtain the approval of the Company's stockholders at a Company Special Meeting and at the time of such failure, any person shall have made a public announcement or otherwise communicated to the Company or its stockholders with respect to an Alternative Proposal with respect to the Company which has not been rejected by the Company and terminated or withdrawn by the party making the Alternative Proposal, then in accordance with *Section 9.3(c)*, immediately prior to such termination in the case of clause (i), or in the case of clause (ii) or (iii) if, within two years following the date of termination, the Company enters into a definitive acquisition, merger or similar agreement to effect an Alternative Proposal upon execution of such agreement, the Company shall pay to Parent an amount equal to Parent's documented Expenses (as defined below) not in excess of $3,000,000 in connection with this Agreement and the transactions contemplated hereby and a termination fee in an amount equal to $42,000,000 (collectively, such Expenses and such fee, the "*Termination Amount*").

(b) Each of Parent and the Company agrees that the payments provided for in *Section 9.3(a)* shall be the sole and exclusive remedy of the parties upon a termination of this Agreement pursuant to *Section 9.1(c), (e)* or *(h)*, as the case may be, and such remedy shall be limited to the payment stipulated in *Section 9.3(a)*; *provided, however*, that nothing in this Agreement shall relieve any party from liability for the willful breach of any of its representations and warranties or the willful breach of any of its covenants or agreements set forth in this Agreement.

(c) Any payment required to be made pursuant to clause (i) of *Section 9.3(a)* shall be made to Parent by the Company immediately prior to the termination of this Agreement and shall be made by wire transfer of immediately available funds to an account designated by Parent.

(d) The parties agree that the agreements contained in this *Section 9.3* are an integral part of the transactions contemplated by the Agreement and constitute liquidated damages and not a penalty. If one party fails to promptly pay to the other any fee due hereunder, the defaulting party shall pay the costs and expenses (including legal fees and expenses) in connection with any action, including the filing of any lawsuit or other legal action, taken to collect payment, together with interest on the amount of any unpaid fee at the publicly announced prime rate of Citibank, N.A. from the date such fee was required to be paid.

(e) For purposes of this Agreement, "Expenses" consist of all out-of-pocket expenses (including all fees and expenses of counsel, accountants, investment bankers, experts and consultants to a party hereto and its affiliates) incurred by a party or on its behalf, in connection with or related to, the authorization, preparation, negotiation, execution and performance of this Agreement, the preparation, printing, filing and mailing of the Proxy Statement and/or any documents relating thereto, the solicitation of stockholder approvals and all other matters relating to the transactions contemplated hereby.

SECTION 9.4 ***Amendment.*** This Agreement may be amended by the Boards of Directors of the parties hereto, at any time before or after approval hereof by the stockholders of the Company and prior to the Effective Time, but after such approval, no such amendment shall (i) alter or change the amount or kind of shares, rights or any of the proceedings of the treatment of shares under Article II, or (ii) alter or change any of the terms and conditions of this Agreement if any of the alterations or changes, alone or in the aggregate, would materially adversely affect the rights of holders of the Company's capital stock, except for alterations or changes that could otherwise be adopted by the Board of Directors of the Company without the further approval of such stockholders. This Agreement may not be amended except by an instrument in writing signed on behalf of each of the parties hereto.

SECTION 9.5 ***Waiver.*** At any time prior to the Effective Time, the parties hereto may (a) extend the time for the performance of any of the obligations or other acts of the other parties hereto, (b) waive any inaccuracies in the representations and warranties contained herein or in any document delivered pursuant hereto and (c) waive compliance with any of the agreements or conditions contained herein, to the extent permitted by applicable law. Any agreement on the part of a party hereto to any such extension or waiver shall be valid if set forth in an instrument in writing signed on behalf of such party.

ARTICLE X

GENERAL PROVISIONS

SECTION 10.1 ***Non-Survival; Effect of Representations and Warranties.*** (a) All representations, warranties and agreements in this Agreement shall not survive the Merger, except as otherwise provided in this Agreement and except for the agreements contained in this *Section 10.1* and in *Article II*, *Section 7.5*, *Section 7.8*, *Section 7.9*, *Section 7.10*, *Section 7.11*, *Section 7.12*, *Section 7.13*, *Section 7.14*, *Section 10.8* and *Section 10.9*.

(b) No party may assert a claim for breach of any representation or warranty contained in this Agreement (whether by direct claim or counterclaim) except in connection with the cancellation of this Agreement pursuant to *Section 9.1(f)(i)* or *Section 9.1(g)(i)* (or pursuant to any other subsection of *Section 9.1* if the terminating party would have been entitled to terminate this Agreement pursuant to *Section 9.1(f)(i)* or *Section 9.1(g)(i)*).

SECTION 10.2 ***Brokers.*** The Company represents and warrants that, except for Morgan Stanley & Co. Incorporated whose fees have been disclosed to Parent prior to the date hereof, no broker, finder or investment banker is entitled to any brokerage, finder's or other fee or commission in connection with the Merger or the transactions contemplated by this Agreement based upon arrangements made by or on behalf of the Company. Parent represents and warrants that, except for Rothschild Inc., prior to the date hereof no broker finder or investment banker is entitled to any brokerage, finder's or other fee or commission in connection with the Merger or the transactions contemplated by this Agreement based upon arrangements made by or on behalf of Parent.

SECTION 10.3 ***Notices.*** All notices and other communications hereunder shall be in writing and shall be deemed given if (i) delivered personally, (ii) sent by reputable overnight courier service, (iii) telecopied (receipt of which is confirmed), or (iv) five days after being mailed by registered or certified mail (return receipt requested) postage prepaid to the parties at the following addresses (or at such other address for a party as shall be specified by like notice):

(a) If to the Company, to:

United Water Resources Inc.
200 Old Hook Road
Harrington Park, NJ 07640

Attention: President
Telephone: (201) 767-2838
Telecopy: (201) 505-0481

with a copy to:

LeBoeuf, Lamb, Greene & MacRae, L.L.P.
125 West 55th Street
New York, New York 10019
Attention: William S. Lamb, Esq.

Telephone: (212) 424-8000
Telecopy: (212) 424-8500

(b) If to Parent or Merger Sub, to:

Lyonnaise American Holding, Inc.
200 Old Hook Road
Harrington Park, NJ 07640

Attention: Mr. Jean Michel Brault,
Executive Vice President

Telephone: (201) 784-7089
Telecopy: (201) 767-2082

with a copy to:

Piper & Marbury L.L.P.
1251 Avenue of the Americas
New York, NY 10020-1104

Attention: Garry P. McCormack, Esq.

Telecopy: (212) 835-6001
Telephone: (212) 835-6000

(c) If to SLDE, to:

Suez Lyonnaise des Eaux
18 Square Edouard VII
75316 Paris Cedex 09
France
Attention: Mr. Gérard Payen, Directeur

Telephone: 33 1.46.95.54.16
Telecopy: 33 1.46.95.40.72

with a copy to:

Piper & Marbury L.L.P.
1251 Avenue of the Americas
New York, NY 10020-1104

Attention: Garry P. McCormack, Esq.

Telephone: (212) 835-6000
Telecopy: (212) 835-6001

SECTION **10.4** ***Miscellaneous.*** This Agreement (including the Disclosure Schedules and the documents and instruments referred to herein) (i) constitutes the entire agreement and supersedes all other prior agreements and understandings, both written and oral, among the parties, or any of them, with respect to the subject matter hereof other than the Confidentiality Agreement, the Governance Agreement and the NARA, each of which remains in full force and effect except as expressly herein modified; (ii) shall not be assigned by operation of law or otherwise; except that Parent or Merger Sub may assign all or any of their rights and obligations hereunder to any wholly-owned subsidiary of Parent; provided that no such assignment shall relieve the assigning party of its obligations hereunder if such assignee does not perform such obligations; and (iii) shall be governed by and construed in accordance with the laws of the State of New Jersey applicable to contracts executed in and to be fully performed in such State, without giving effect to its conflicts of law, rules or principles and except to the extent the provisions of this Agreement (including the documents or instruments referred to herein) are expressly governed by or derive their authority from the NJBCA.

SECTION 10.5 ***Interpretation.*** When a reference is made in this Agreement to Sections or Exhibits, such reference shall be to a Section or Exhibit of this Agreement, respectively, unless otherwise indicated. The table of contents and headings contained in this Agreement are for reference purposes only and shall not affect in any way the meaning or interpretation of this Agreement. Whenever the words "include", "includes" or "including" are used in this Agreement, they shall be deemed to be followed by the words "without limitation".

SECTION 10.6 ***Counterparts; Effect.*** This Agreement may be executed in one or more counterparts, each of which shall be deemed to be an original, but all of which shall constitute one and the same agreement.

SECTION 10.7 ***Parties in Interest.*** This Agreement shall be binding upon and inure solely to the benefit of each party hereto, and, except for rights of Indemnified Parties as set forth in *Section 7.5*, nothing in this Agreement, express or implied, is intended to confer upon any other person any rights or remedies of any nature whatsoever under or by reason of this Agreement.

SECTION 10.8 ***Waiver of Jury Trial and Certain Damages.*** Each party to this Agreement waives, to the fullest extent permitted by applicable law, (i) any right it may have to a trial by jury in respect of any action, suit or proceeding arising out of or relating to this Agreement and (ii) except as expressly set forth in this Agreement (including, but not limited to, *Section 9.3* hereof), any right it may have to receive damages from any other party on any claim arising out of this Agreement (but not any other agreement the parties to which include any or all parties to this Agreement) based on any theory of liability for any special, indirect, consequential (including lost profits) or punitive damages.

SECTION 10.9 ***Enforcement.*** The parties agree that irreparable damage would occur in the event that any of the provisions of this Agreement were not performed in accordance with their specific terms or were otherwise breached. It is accordingly agreed that the parties shall be entitled to an injunction or injunctions to prevent breaches of this Agreement and to enforce specifically the terms and provisions of this Agreement in any United States federal state court located in the States of New Jersey, New York or Delaware, this being in addition to any other remedy to which they are entitled at law or in equity. In addition, each of the parties hereto (a) consents to submit itself to the exclusive personal jurisdiction of any federal or state court located in any of the States of New Jersey, New York or Delaware solely with respect to any dispute arising out of this Agreement or any of the transactions contemplated by this Agreement, (b) agrees that it will not attempt to deny such personal jurisdiction by motion or other request for leave from any such court and (c) agrees that it will not bring any action relating to this Agreement or any of the transactions contemplated by this Agreement in any court.

SECTION 10.10 ***Severability.*** If any term or other provision of this Agreement is determined by a court of competent jurisdiction to be invalid, illegal or incapable of being enforced by any rule of law, or public policy, all other conditions and provisions of this Agreement shall nevertheless remain in full force and effect so long as the economic or legal substance of the transactions contemplated hereby is not affected in any manner materially adverse to any party. Upon such determination that any term or other provision is invalid, illegal or incapable of being enforced, the parties hereto shall negotiate in good faith to modify this Agreement so as to effect the original intent of the parties as closely as possible in a mutually acceptable manner in order that the transactions contemplated hereby be consummated as originally contemplated to the fullest extent possible.

ARTICLE XI

PROVISIONS RELATING TO SLDE

SECTION 11.1 ***Organization and Authority.*** SLDE is a société anonyme duly organized and validly existing under the laws of the Republic of France and has full power, corporate or otherwise, to execute and deliver and to perform all of its obligations contained in *Section 11.2* of this Agreement. The execution and delivery of this Agreement by SLDE and the performance by SLDE of its obligations hereunder have been duly authorized by all necessary action on behalf of SLDE, and this Agreement has been duly and validly executed and delivered by SLDE and, assuming the due authorization, execution and delivery hereof by the other signatories hereto, constitutes the valid and binding obligation of SLDE enforceable against it in accordance with its terms.

SECTION 11.2 ***Obligations of SLDE.*** SLDE agrees (i) to cause Parent and Merger Sub to have at the Closing sufficient funds to consummate the transactions contemplated by this Agreement at the Closing, and (ii) to cause Parent and Merger Sub to have sufficient funds to meet all of their other financial obligations under or related to this Agreement.

[REMAINDER OF PAGE INTENTIONALLY BLANK]

IN WITNESS WHEREOF, the Company, Parent, Merger Co. and SLDE have caused this Agreement to be signed by their respective officers thereunto duly authorized as of the date first written above.

UNITED WATER RESOURCES INC.

By: /s/ DONALD L. CORRELL
Name: Donald L. Correll
Title: Chairman and CEO

Attest: /s/ MICHAEL C. J. FALLON

LYONNAISE AMERICAN HOLDING, INC.

By: /s/ JEAN MICHEL BRAULT
Name: Jean Michel Brault
Title: Executive Vice President

Attest: /s/ GARRY P. MCCORMACK

LAH ACQUISITION CO.

By: /s/ JEAN MICHEL BRAULT
Name: Jean Michel Brault
Title: President

Attest: /s/ GARRY P. MCCORMACK

SUEZ LYONNAISE DES EAUX

By: /s/ GÉRARD PAYEN
Name: Gérard Payen
Title: Executive Vice President -Water

Attest: /s/ JEAN-PAUL MINETTE

[Letterhead of Morgan Stanley & Co. Incorporated]

ANNEX B

August 20, 1999

Board of Directors
United Water Resources
200 Old Hook Road
Harrington Park, NJ 07640-1799

Members of the Board:

We understand that United Water Resources Inc. ("UWR" or the "Company"), Lyonnaise American Holding, Inc. ("LAH"), LAH Acquisition Co., a wholly owned subsidiary of LAH ("LAH Acquisition Co.") and solely with respect to certain of LAH's obligations, Suez Lyonnaise des Eaux, a French Société Anonyme ("Suez"), the parent of LAH, propose to enter into an Agreement and Plan of Merger, substantially in the form of the draft dated August 20, 1999 (the "Merger Agreement"), which provides, among other things, for the merger (the "Merger") of LAH Acquisition Co. with and into UWR. Pursuant to the Merger, UWR will become a wholly owned subsidiary of LAH and each outstanding share of common stock, no par value per share (the "Common Stock"), of UWR, together with the associated right to purchase shares of 5% Series A Cumulative Convertible Preference Stock, no par value, of UWR (the "Series A Preference Stock"), other than shares and rights held in treasury or held by LAH or any affiliate of LAH and UWR, will be converted into the right to receive $35.00 per share in cash, an additional dividend of $0.06 per share in each of the first three fiscal quarters after announcement and a special dividend payable at closing of the difference between $0.48 and the additional dividends paid, all as described in the Merger Agreement (collectively the "Consideration"). Additionally, pursuant to the Merger, each outstanding share of Series A Preference Stock, other than shares held in treasury or held by LAH or any affiliate of LAH and UWR, shall be converted into the right to receive $35.00 per share in cash multiplied by the number of shares of Common Stock issuable upon the conversion of a share of Series A Preference Stock. The terms and conditions of the Merger are more fully set forth in the Merger Agreement. We further understand that approximately 32% of the outstanding shares of the Common Stock is owned by LAH and its affiliates.

You have asked for our opinion as to whether the Consideration to be received by the holders of shares of Common Stock pursuant to the Merger Agreement is fair from a financial point of view to such holders other than LAH and its affiliates.

For purposes of the opinion set forth herein, we have:

(i) reviewed certain publicly available financial statements and other information of UWR;

(ii) reviewed certain internal financial statements and other financial and operating data concerning UWR prepared by the management of UWR;

(iii) reviewed certain financial projections prepared by the management of UWR;

(iv) discussed the past and current operations and financial condition and the prospects of UWR with senior executives of UWR;

(v) reviewed the proforma impact of the Merger on Suez's earnings per share, consolidated capitalization and financial ratios;

(vi) reviewed the reported prices and trading activity for the Common Stock;

(vii) compared the financial performance of UWR and the prices and trading activity of the Common Stock with that of certain other comparable publicly-traded companies and their securities;

(viii) reviewed the financial terms, to the extent publicly available, of certain comparable acquisition transactions;

(ix) participated in discussions and negotiations among representatives of UWR, LAH and Suez and their financial and legal advisors;

(x) reviewed certain material agreements between UWR and LAH;

(xi) reviewed the draft Merger Agreement and certain related documents; and

(x) performed such other analyses and considered such other factors as we have deemed appropriate.

We have assumed and relied upon without independent verification the accuracy and completeness of the information reviewed by us for the purposes of this opinion. With respect to the financial projections, we have assumed that they have been reasonably prepared on bases reflecting the best currently available estimates and judgments of the future financial performance of UWR. We have not made any independent valuation or appraisal of the assets or liabilities of UWR. Our opinion is necessarily based on financial, economic, market and other conditions as in effect on, and the information made available to us as of, the date hereof.

In arriving at our opinion, we were not authorized to solicit, and did not solicit, interest from any party with respect to the acquisition of UWR or any of its assets, nor did we negotiate with any of the parties, other than LAH and Suez.

We have acted as financial advisor to the Board of Directors of UWR in connection with this transaction and will receive a fee for our services. Morgan Stanley and its affiliates have provided and continue to provide financial advisory and financing services to Suez and/or its affiliates and have received and will receive fees for the rendering of these services.

It is understood that this letter is for the information of the Board of Directors of UWR, except that this opinion may be included in its entirety in any filing made by UWR in respect of the transaction with the Securities and Exchange Commission. In addition, Morgan Stanley expresses no opinion or recommendation as to how the shareholders of UWR should vote at the shareholders' meetings held in connection with the Merger.

Based upon and subject to the foregoing, we are of the opinion on the date hereof that the Consideration to be received by the holders of shares of Common Stock pursuant to the Merger Agreement is fair from a financial point of view to such holders other than LAH and its affiliates.

Very truly yours,

MORGAN STANLEY & CO. INCORPORATED

By: /s/

Daniel B. More
Managing Director

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NOTE: Please date and sign exactly as name appears hereon. When shares are held by joint tenants both should sign. (Executors, Administrators, Trustees, etc. should so indicate).

. FOLD AND DETACH HERE .

VOTE BY TELEPHONE

[GRAPHIC] QUICK ... EASY ... IMMEDIATE [GRAPHIC]

YOUR VOTE IS IMPORTANT! - YOU CAN VOTE IN ONE OF TWO WAYS:

1. TO VOTE BY PHONE: Call toll-free [____________] on a touch tone telephone 24 hours a day-7 days a week

There is NO CHARGE to you for this call. - Have your proxy card in hand.

You will be asked to enter a Control Number, which is located in the box in the lower right hand corner of this form

[Insert instructions]

or
--

2. VOTE BY PROXY: Mark, sign and date your proxy card and return promptly in the enclosed envelope.

NOTE: If you vote by telephone, THERE IS NO NEED TO MAIL BACK your Proxy Card.

PROXY

UNITED WATER RESOURCES INC.

PROXY FOR SPECIAL MEETING OF STOCKHOLDERS-___________, 1999

The undersigned stockholder of United Water Resources Inc. ("UWR") hereby constitutes and appoints LAWRENCE R. CODEY, PETER DEL COL and MARCIA L. WORTHING, or any of them, the attorneys or attorney and proxies or proxy of the undersigned, with full power of substitution and revocation, for and in the name of the undersigned, to attend the Special Meeting of Stockholders of UWR to be held at ____________________, New Jersey ____________________, on ____________________, 1999, at _____a.m., and any adjournment or adjournments thereof, receipt of the notice of which meeting stating the purposes thereof being hereby acknowledged, to vote all of the shares of UWR which the undersigned would be entitled to vote if then personally present as follows:

(Continued and to be signed on other side)

. FOLD AND DETACH HERE .

Dear Stockholder(s) of United Water Resources Inc.:

Enclosed you will find materials regarding the United Water Resources Inc., [ ],1999, Special Meeting of Stockholders. The notice of the Special Meeting and proxy statement describe the formal business to be transacted at the meeting as summarized on the attached proxy card.

Whether or not you expect to attend the Special Meeting, please complete and return promptly the attached proxy card in the accompanying envelope, which requires no postage if mailed in the United States. You may vote your proxy by telephone. If you vote by telephone, there is no need to mail back your proxy card. As a stockholder, please remember that your vote is important to us. We look forward to hearing from you.

[Image]

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United Water [LOGO]\(R)\

1999 Special Meeting
Location: ____________________

The ________________________ is accessible via ________________________. From Exit ramp turn ________________________............

FROM NEW JERSEY & SOUTH: Take ________________________

FROM NEW YORK CITY: Take ________________________

FROM UPSTATE NEW YORK. Take ________________________

[MAP OF ________________________ APPEARS HERE]

This Proxy Is Solicited On Behalf Of The Board of Directors

Please mark your votes as indicated in this example [X]

		FOR	AGAINST	ABSTAIN
1.	To Adopt and Approve The Agreement and Plan of Merger, dated as of August 20, 1999, by and among United Water Resources, Inc., Lyonnaise American Holding, Inc., LAH Acquisition Co., and Suez Lyonnaise des Eaux.	[_]	[_]	[_]

2. To vote all of such shares as they or he or she may deem proper upon all other matters that may properly come before said meeting and any adjournments thereof.

Mark box if you plan to attend the Special Meeting [_]

This Proxy is given and is to be construed under the laws of the State of New Jersey and will be voted "FOR" the merger agreement if the undersigned has not specified a choice in the spaces provided therefore. This proxy when properly executed will be voted in the manner directed herein by the undersigned.

Signature(s) of Stockholder(s)________________________________ Date____________, 1999

EXHIBIT F

COMPLIANCE WITH DEP STANDARDS

After reasonable investigation, the systems owned by United Water Resources, Inc. ("systems") appear to be in satisfactory condition and in compliance with all applicable standards set by the Florida Department of Environmental Protection ("DEP"). The systems have no outstanding Notices of Violations of any standard(s) set by the DEP or any outstanding consent orders with DEP.

EXHIBIT G

AFFIDAVIT REGARDING NOTICE BY MAIL (NON-CUSTOMERS)

This will be a late-filed Exhibit.

EXHIBIT H

AFFIDAVIT REGARDING NOTICE BY MAIL (CUSTOMERS)

This will be a late-filed Exhibit.

EXHIBIT I

AFFIDAVIT REGARDING PUBLISHED NOTICE

This will be a late-filed Exhibit.

EXHIBIT J

REAL PROPERTY OF UNITED WATER FLORIDA, INC.

United Water Florida, Inc. owns or has long-term leases on the land where its utility treatment facilities are located. The proposed merger between United Water Resources, Inc. and Lyonnaise American Holding, Inc. will have no effect on the real property of United Water Florida, Inc. That is, there will be no conveyance of real property, no change in title ownership, no lien imposed and no modifications to the existing deeds or leases. Since the proposed merger of United Water Florida, Inc.'s grandparent corporation does not effect the real property of United Water Florida, Inc., no further evidence of ownership is attached.

EXHIBIT K

TARIFF SHEETS

Because this transaction involves a merger of United Water Resources, Inc., the grandparent corporation of United Water Florida, Inc., no changes in the company name, rates, conditions of service or officers of United Water Florida, Inc. are expected. Therefore, no revised tariff sheets are attached.

EXHIBIT L

The Commission is currently revising the original certificates held by United Water Florida, Inc. Thus, they are not available for attachment to this Application. The certificates held by United Water Florida, Inc. do not need to be revised as a result of this transaction.

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