

BRITISH NUCLEAR FUELS plc
Company No: 1002607

Annual Report & Accounts

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Preface

The nuclear industry in the UK has been operating for nearly 60 years. Today it faces its greatest ever change as the Government steps up its programme to decommission Britain's nuclear power stations and clean-up the legacy of this long history. With the introduction of a new competitive market for carrying out the task, the industry faces huge challenges.

This is the story of how BNFL is changing.

The story so far

British Nuclear Fuels Ltd was formed by the UK Government in 1971. At the time, its main activities were nuclear fuel services and the operation of two nuclear power stations for generating electricity. BNFL became a public limited company in 1984. Recent years have brought rapid growth. We acquired

our biggest customer, Magnox Electric plc, from the UK Government in 1998 and bought Westinghouse Electric Company the following year. In 2000 we acquired the worldwide nuclear businesses of ABB, a move that enabled us to offer a much broader range of services in the United States, Europe and Asia. Today we are an international business employing 23,000 people in 16 countries and serving governments and nuclear utilities around the globe. Our work spans the entire nuclear energy cycle from reactor design and fuel manufacture to decommissioning nuclear power stations and cleaning up nuclear sites.

As we prepare for the launch of the Nuclear Decommissioning Authority (NDA) we have been reorganising our UK business to reflect the challenges and the opportunities ahead of us.

Our main priority is to ensure the successful establishment of British Nuclear Group, which will specialise in nuclear decommissioning and clean-up.

Activities of BNFL

- **Decommissioning and clean-up services.** Over the last 30 years, BNFL has successfully closed down and cleaned up over 50 redundant nuclear facilities in the UK, Europe and the United States. With this long experience, it is now an international leader in decommissioning and decontamination. Along the way it has pioneered sophisticated technologies for handling nuclear waste – these ranging from robotics to waste encapsulation. As the emphasis in the UK switches to decommissioning and clean-up, BNFL's unique skills in these areas will be invaluable.
- **Designing reactors, manufacturing nuclear fuel and supplying services to help nuclear utilities run their plants safely and efficiently.** BNFL is one of the leading forces in this £2.5 billion-a-year market. Additionally the Westinghouse AP1000 reactor design is going through the licensing process with the Nuclear Regulatory Commission in the United States.
- **Generating electricity.** BNFL runs the five Magnox nuclear power stations still operating in the UK. These currently supply about 6% of the UK's electricity.
- **Managing the recycling of used reactor fuel.** The commercial interface with utility customers together with the transport of used fuel and nuclear waste is managed by Spent Fuel Services. The recycling and waste handling plants are operated by British Nuclear Group.

A major reason for BNFL's success is its reputation for operating safely and with due care for the environment. Safety and environmental considerations govern all its activities, helping BNFL not just to meet its regulatory obligations but to keep setting new standards for the industry.

Success also depends on the quality of BNFL's people. Our workforce is one of the most highly trained and qualified in the worldwide industry, offering long experience and a unique combination of scientific, technical and engineering skills.

A new chapter for the UK nuclear industry

BNFL is responsible for decommissioning the majority of Britain's civil nuclear sites and cleaning up the legacy of its nuclear programme. Many of these sites date back to the 1940s and 50s, long before the formation of BNFL. While meeting this responsibility has helped to make BNFL a world leader in the field, it imposes a heavy financial cost. The financial impact of these historic liabilities are at odds with the financial performance of a commercial company. They distort BNFL's true trading performance and keep the business in loss. In 2002, the UK Government set out new arrangements for cleaning up Britain's nuclear legacy with the publication of its White Paper, 'Managing the Nuclear Legacy – a Strategy for Action'. This proposed the creation of a new national body, the NDA, to take responsibility for the majority of the UK's civil nuclear assets and liabilities.

In 2003, the Government published its Energy Bill to implement the White Paper and pave the way for setting up the NDA. The aim was to put in place a system that would deal with Britain's nuclear liabilities as quickly and efficiently as possible, combining best value for the taxpayer with due regard to safety, security and care for the environment. Above all, the new regime had to be 'open, transparent and command public confidence'.

We expect the Energy Bill to become law in the summer of 2004 and the NDA will begin operating on 1 April 2005. On that date, the NDA will take ownership of the majority of Britain's nuclear assets, including Sellafield, Springfields and the Magnox power stations currently run by BNFL and be responsible for the necessary decommissioning and clean-up. The work itself will be opened up to competitive tender in due course with each facility operated by a site licensee company with senior management supplied by the successful contracting company. Until then, the Government's Liabilities Management Unit (LMU) will continue to manage the transition.

This proposed transfer of assets and removal of liabilities from the balance sheet is good news for BNFL. Instead of owning and operating its own sites, BNFL will become a contractor, competing with others for decommissioning and clean-up contracts from the NDA with the opportunity to earn fees based on how well it performs against demanding targets.

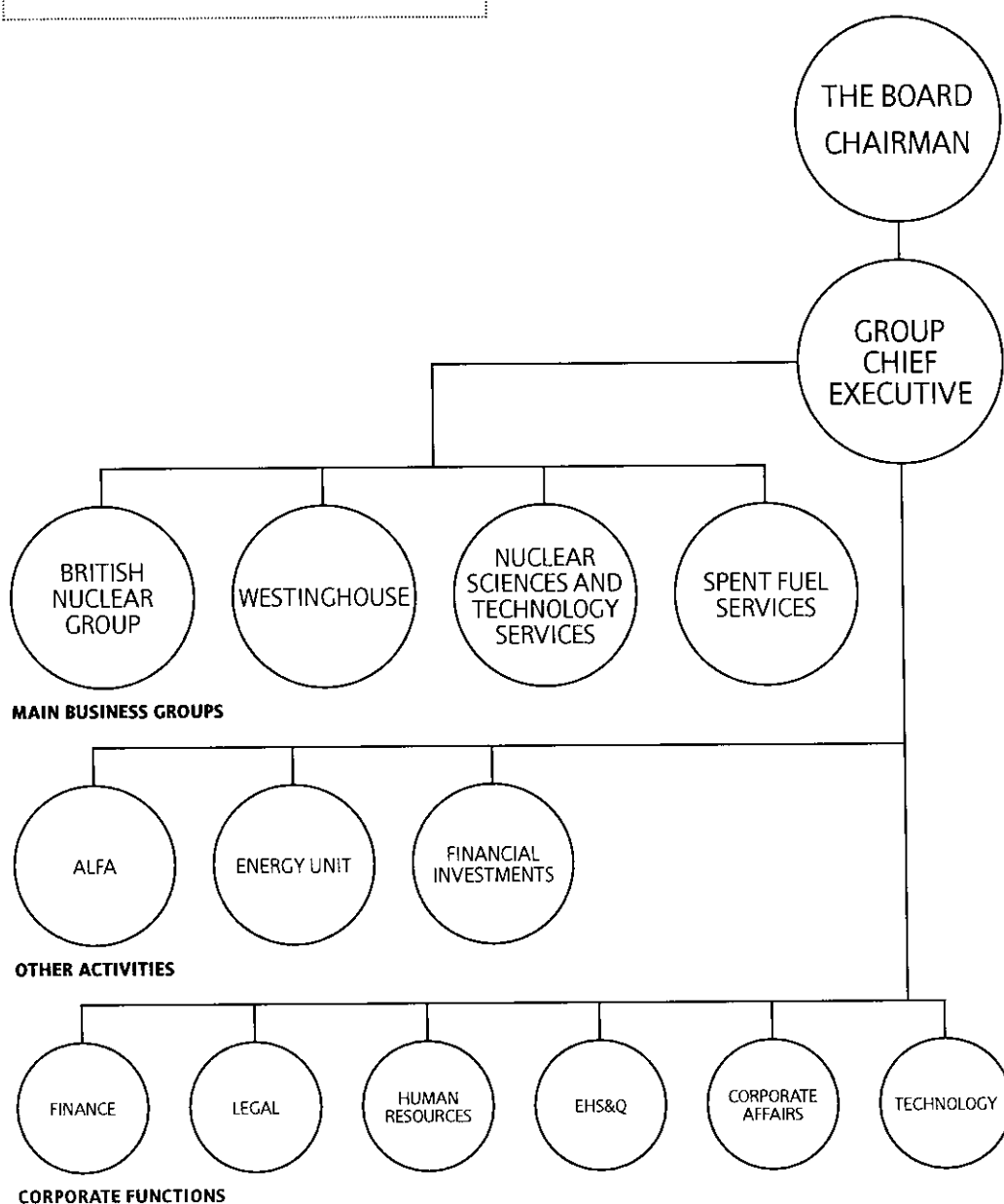
Given that BNFL would need to change, the Government announced a joint strategic review in July 2003. Between then and December, the Government and BNFL jointly examined the implications of the new regime and BNFL's future strategic options.

The review concluded that BNFL's main focus will be the decommissioning and clean-up of Britain's nuclear facilities and the safe, expert handling of the resultant waste. This work will be carried out by a new BNFL business that will draw together the company's technical expertise in these areas and introduce the commercial and management skills that will make BNFL an effective competitor. Known as British Nuclear Group, the new business is already operating in shadow form and will be formally established on the same day as the NDA on 1 April 2005.

The new BNFL

The new BNFL is structured to reflect the outcome of the joint strategic review with the UK Government. Comprising four self standing customer facing business groups including: British Nuclear Group, Westinghouse, Nuclear Sciences and Technology Services and Spent Fuel Services, each with its own management being responsible for its own profitability. BNFL ALFA, the Energy Unit and our financial investments in organisations such as Urenco make up our other activities. These are all supported by six Group corporate functions: finance; legal; human resources; environment, health, safety and quality; corporate affairs and technology.

THE NEW BNFL STRUCTURE



Challenges and opportunities

When the NDA takes responsibility for the majority of Britain's nuclear assets on 1 April 2005, it will demand the best decommissioning and clean-up services that the worldwide nuclear industry can offer. The work, furthermore, will need to be carried out quickly, cost-effectively and to the highest safety and environmental standards. For the successful contractor the main prize will be the cleaning up of Sellafield, one of the UK's biggest ever public sector contracts. The nuclear clean-up market as a whole is estimated to be worth £2 billion a year in the UK.

With our long record in decommissioning and clean-up, we are well placed to win a large share of the UK market. That said, the competition will be intense and BNFL has a major task on its hands to be ready for the new regime in the UK. Between now and the NDA launch date, its main focus is on building a business that is not only technically qualified to do the job but also has the financial and commercial expertise to compete successfully. The aim is that British Nuclear Group should eventually become a viable and profitable nuclear site management company.

All this requires a transformation from a business that has always owned and operated its own facilities, to one that has few assets other than its people and succeeds by selling its skills and meeting its contractual obligations.

The challenge, now, is to match these credentials with a sharper competitive edge. Success will depend on being faster, smarter and safer than the competition and on meeting the customer's demands on time and on budget.

To this end, British Nuclear Group is working hard to attract the right skills; install the right systems and management; streamline its operations; manage its costs; improve efficiency; instil a customer focused culture and become in every way like the commercial organisation it intends to be. Since April 2002 it has answered to BNFL ALFA, its internal customer and forerunner of the NDA and has had to meet increasingly stringent targets. Its performance has measurably improved over this period.

The launch of the new British Nuclear Group identity in May 2004 was a powerful signal that BNFL accepts the challenge and will be ready, when the time comes, to provide the very best service to the NDA.

In the global marketplace, Westinghouse continues to compete for nuclear fuel and reactor services contracts and is making progress in obtaining approval from the US Nuclear Regulatory Commission for its advanced AP1000 reactor. Its record of competitive expertise and commercial success is one that British Nuclear Group intends to emulate.

BNFL's entire operation is underpinned by strong common values that commit the business to:

BNFL VALUES >	ACT WITH INTEGRITY AND RESPECT FOR OTHERS	BE SAFE AND ENVIRONMENTALLY RESPONSIBLE
COMMIT TO ACHIEVE SUCCESS FOR OUR CUSTOMERS	DELIVER VALUE AND PROFIT	EXCEL IN OUR OPERATIONS

Nuclear energy in the future

Although the plan is to shut down the present generation of nuclear power plants and clean up the country's nuclear legacy, BNFL believes the industry should be ready for any changes of nuclear policy in the future. In the face of global warming and pressure to cut carbon emissions, the Government is looking increasingly at non-CO₂ sources of

energy. Its 2003 White Paper 'Our energy future – creating a low-carbon economy', foresees a greater role for renewable sources such as wind power, backed by rising imports of gas from countries such as Russia and Algeria. It also speaks of 'keeping the nuclear option open' should a new-build programme become necessary.

If the Government is to meet its CO₂ reduction targets while also ensuring security of supply and constant baseload generation, it is likely to need nuclear energy in the future. Other countries have come to the same conclusion and are stepping up their nuclear programmes as the only way to ensure secure, reliable, carbon-free energy. Today, nuclear energy provides about 16% of the world's electricity. Over 440 nuclear reactors now operate in 30 countries and at least 33 further reactors are under construction. More are planned or being considered in countries such as the United States, South Korea, China and Finland.

The primary role of Nuclear Sciences and Technology Services (NSTS) is to sell services to the NDA and help to nurture the UK's long-term nuclear capability. In addition through Westinghouse, we own the latest reactor technology – the AP1000 – that will help to make nuclear generation more efficient and cost-competitive. We also have an active programme of research projects including collaborations with international partners to develop new generations of reactors. To encourage academic research and a flow of talent into the industry, we maintain links with 35 UK universities.

In these ways, BNFL will not only meet the Government's immediate objective of cleaning up the nuclear industry, but be ready to play its part in Britain's long-term energy generation.

Chairman's statement

I step down as Chairman with BNFL well prepared for the future. The recent strategic review has provided clear direction and consensus with the UK Government on what our role should be. With the advent of the Nuclear Decommissioning Authority, we welcome the chance to apply our skills in the new, competitive marketplace. We look forward to offering the best possible service to our customers and real value to our Shareholder.

Looking for new opportunities...

We have been working closely with the UK Government to assess the strategic implications for BNFL and the company's future direction. The key change internally has been the formation of British Nuclear Group to be the focus of our clean-up skills and to bring a new commercial and competitive edge to these operations.

These changes have involved an immense amount of work. Our new Chief Executive, Mike Parker, became involved in the joint strategic review with the Government as soon as he joined the company in August 2003 and I congratulate him and his management team on a successful outcome. The Board was pleased to welcome Mike to the company last year and he has our full support as he leads BNFL into the new, competitive marketplace.

The new reorganised Group provides every opportunity for BNFL to succeed. The proposed transfer of our UK nuclear assets and liabilities to the NDA on 1 April 2005 will remove the primary cause of our losses in recent years, leaving BNFL to manage a portfolio of nuclear services and fuel businesses going forward. British Nuclear Group is well positioned to compete for major contracts in the UK. With further contributions from Westinghouse, Spent Fuel Services and our Sciences and Technology operation, we expect to see a strong and profitable BNFL in the coming years.

Results

BNFL's results will inevitably be distorted until the NDA takes responsibility for the legacy issues, as well as a significant portion of our assets and liabilities. This year's losses before taxation stood at £299 million due to higher costs at Sellafield, continuing losses in electricity generation and delays in starting up our MOX production. On the other hand, our operating performance has been outstanding with higher reprocessing and vitrification throughput at our Thorp and Magnox plants, a 5% increase compared to target in electricity generation from our Magnox stations and more major contracts for Westinghouse from customers around the world. It is also pleasing that we achieved these results with ever-higher standards of safety, security and environmental performance.

The strategy review and subsequent work with the DTI have further developed the business model on which BNFL will operate post-NDA. We are confident that once these changes take effect and the NDA transfer is completed, we will have a viable group based on a set of independent businesses. The Group is expected to be profitable, tax paying and in a position after 2005 to pay dividends for the first time in several years.

Five years of progress

I announced in November 2003 that I intended to step down as Chairman in the first half of 2004. As this is my last Chairman's statement, I feel it appropriate to review the achievements of the last five years.

I joined BNFL at a troubled time in its history and was obliged, almost immediately, to replace the Board and appoint a new Chief Executive – Norman Askew. Since then, enormous strides have been made in transforming BNFL. From the public sector mentality of five years ago, we've become more commercial and competitive, more financially aware and more responsive to the needs of the customer.

Nor should we underestimate our progress in changing the culture at Sellafield. No company addressing the kind of situation we faced at Sellafield could hope to make lasting changes without the co-operation of unions and employees. But change has been achieved and is well reflected in the operational performance for this year. There is still much to be done, but we now have a much better base on which to build as we move from being the site owner to the site contractor.

In Westinghouse meanwhile, we have a world-class business that is well managed and in pole position to be a key participant if the authorities in the United States and Europe begin a new programme of building nuclear power stations. It has recently joined seven major plant operators and another nuclear reactor vendor to form a consortium that will work with the US Department of Energy to demonstrate and test a new licensing process for obtaining a combined construction and operating licence for advanced nuclear power reactors. In addition, Westinghouse

is well established in the Far East for any opportunities that may arise there. We now need to focus on gaining value from Westinghouse and our other overseas activities.

When a company's reputation suffered as ours did in 1999-2000, all aspects of the business are affected in different ways. The awarding in 2000 of the Aldermaston Weapons Establishment (AWE) decommissioning contract, in partnership with Lockheed Martin and Serco, was therefore very important to our Environmental Services business. Last year's 15-year extension to the 10-year contract shows how well this team has performed and indicates a unique capability which should be used in the future in the multi-billion dollar global decommissioning and clean-up market. Keeping these skills together is just as important for BNFL as retaining our science and technology capability.

Our research and technology team has excelled over the past few years and the recent co-operation agreements with several UK universities (particularly the University of Manchester Institute of Science and Technology) underlines the importance of having a high skills base for science and technology in the nuclear industry. This is essential, not only to meet the UK Government's requirement to keep the nuclear option open, but also to deal with complex issues such as the abatement of Technetium-99 discharges from Sellafield. The recently announced breakthrough on this issue will reduce discharges by 90%.

Elsewhere, we've re-established our business relationships with some of our key customers, particularly the Japanese utilities who themselves have had major operational and public perception problems, and also British Energy in its period of instability.

We've also made a determined effort to rebuild trust by communicating openly and transparently with our stakeholders. The present emphasis on corporate social responsibility (CSR) and our continuing improvements in health and safety are further evidence of the changes that have taken place. In particular, I was very pleased with the publication in 2003 of our first-ever CSR report and the response it has had from our stakeholders.

Looking forward

Although we are pleased that BNFL can now look forward to a successful future in decommissioning and clean-up, the nuclear energy industry will continue to face uncertainty until the UK Government formulates a long-term energy policy. The 2003 Energy White Paper speaks only of 'keeping the nuclear option open' as part of the Government's commitment to renewable sources of energy. While renewables have their place, they do not, on their own, solve the issues of global warming and the security of Britain's energy supplies in years to come. Nuclear power offers important benefits on both counts while providing the baseload energy generation that renewables cannot and potentially reducing our reliance on imported gas.

Few of our supporters and critics appreciate that, with twenty-first century technology, nuclear energy could supply 25% of the UK's electricity requirement from just ten new reactors on three existing nuclear power station sites. Nuclear waste from these modern reactors would be reduced by 85%, the price of electricity would be competitive with gas and the electricity baseload would be guaranteed with more than 90% utilisation at all times. This would ensure ongoing security of supply for the UK and help the country to meet its commitment to reduce emissions and greenhouse gases. All this is technically possible, but the UK now needs to take the strategic decision to adopt a balanced energy policy and to agree the method for handling historic and future nuclear waste. Without this decision, the UK's future energy supplies will remain at risk.

We recognise that any such decision will be politically difficult. We see our task therefore, as providing the NDA with the best possible service in decommissioning and clean-up while keeping alive the skills that will be needed if the Government should decide to embark on a nuclear rebuilding programme. We have agreed the future direction of our utilities and other businesses. We now need to address their successful development and communicate these plans to all our stakeholders on an on-going basis.

A new chapter

It was a great pleasure to be able to announce the appointment of Gordon Campbell as the new Chairman of BNFL.

Gordon Campbell inherits a business whose strength lies in the expertise and dedication of its 23,000 employees around the world. Our people are a highly skilled and committed team and I am personally very grateful for their support and hard work over the years.

My tenure as Chairman has been demanding but also satisfying and extremely worthwhile. I wish the Board and the company all the best for the future and leave with every confidence that BNFL will more than measure up to the challenges and opportunities that lie ahead.

Hugh Collum Chairman

Gordon Campbell (57)

Non-Executive Director Joined the Board on 1 August 2000. He is part-time Chairman of Babcock International Group PLC and former Chief Executive of Courtaulds plc. He is a Vice-President of the Royal Academy of Engineering, Non-Executive Chairman of ITI Scotland and a Non-Executive Director of Jupiter Split Trust plc. He has been appointed Non-Executive Chairman of BNFL commencing 1 June 2004.

Chief Executive's review

The UK Government has taken a bold step in its radical reshaping of Britain's nuclear industry.

BNFL's response is similarly bold, the creation of British Nuclear Group and the transformation of its organisation and culture to allow us to play a leading role in the safe, cost-effective and timely management of the UK's nuclear clean-up programme.

Looking for new challenges...

The period since last summer has been one of the most challenging in BNFL's history. The Secretary of State announced in July 2003 that the Government and BNFL had agreed to carry out a joint review of BNFL's future strategy.

Completed in December, this review examined future options for BNFL in the light of the 2002 White Paper, 'Managing the Nuclear Legacy – A Strategy for Action'. This put the focus firmly on the clean-up and decommissioning of nuclear sites and laid down a challenge to the UK industry. It told us to sharpen our commercial skills, become more competitive and show we were capable of carrying out the Government's clean-up programme safely, cost-effectively and on schedule. Furthermore, we needed to be ready for the challenge by 1 April 2005 when the majority of our UK nuclear assets and liabilities are due to pass to the Nuclear Decommissioning Authority alongside the associated legacy issues, BNFL would then become a contractor. In due course, the UK nuclear clean-up programme would start to be run by competitive tender. During this time we will continue to serve all our existing customers and maintain our high standards of service.

The future BNFL

The strategic review and the formation of the NDA represent the biggest change ever to hit the UK nuclear industry. It affects our structures, the way we measure performance, the skills we need, our accountabilities, decision-making and much more. In particular, it requires us to move from an owner-operator of nuclear sites to a commercial business competing for NDA contracts. Responding to these requirements has meant an immense amount of work and a radical re-think of the way we operate whilst keeping the safety of our operations as our number one priority.

To begin with, we've changed our structure from two business groups – Nuclear Utilities Group and Government Services Group – to four self-standing businesses. These are: British Nuclear Group, Westinghouse, Nuclear Sciences and Technology Services and Spent Fuel Services, each with its own management structure and with a clear responsibility for their own profit and loss. In the past the corporate centre has directly managed BNFL's UK

operations. It is now reduced in size and will concentrate on providing strategic direction for the businesses as well as reviewing, challenging and ensuring high levels of performance. In light of this and the introduction of the NDA we are also reviewing the Group legal structure.

Our biggest task to date has been the setting up of the British Nuclear Group, formerly known as Government Services. This specialist clean-up business will act as contractor and site management company to the NDA. British Nuclear Group became fully operational in just six months and was formally launched in May 2004 under the leadership of Lawrie Haynes.

It's a huge task, but Lawrie and his team are working very hard in drawing together BNFL's considerable strengths in nuclear clean-up and melding them into a new organisation. Perhaps the greatest challenge is to move beyond the old monopoly mindset and create a culture that is competitive, commercially astute and focused on the customer – not least, by introducing new commercial and management skills. With BNFL ALFA acting as both coach and customer, British Nuclear Group has already shown it can meet rigorous commercial demands as well as technically performing well in managing and operating our assets.

That said, there is much work yet to be done to prepare British Nuclear Group for the future. As well as completing its own internal transformation, the business still needs to agree with the Government precisely how NDA contracts will operate, both in the period immediately after 1 April 2005 and later on when the UK clean-up market is thrown open to competitive tender.

The strategic review also addressed the future of the other parts of BNFL.

- Spent Fuel Services (SFS) will continue to manage recycling contracts with the utility customers on behalf of the NDA.
- Nuclear Sciences and Technology Services (NSTS) will offer BNFL's research and technology resource on a commercial basis to site managements, the NDA and other customers.

- These businesses along with the Springfields facility in the UK which will initially be managed by Westinghouse under contract to the NDA, have also started making changes in preparation for the competitive marketplace. They are now looking, with the Government, at how markets and contracts will be structured under the NDA.
- For its part, Westinghouse will have greater financial independence so as to open up the possibility of future private sector participation.

Following these extensive changes, we've also been reviewing decision making accountabilities between the corporate centre and the businesses. This has led to the redesigning of the processes, roles and responsibilities including the review process used to assess the effectiveness of our business performance. In parallel the distribution of accountabilities between all the stakeholders including Chairman, Chief Executive and the Board were also reviewed. It all adds up to a massive programme of work and change to ensure we are ready to compete when the time comes.

How we've done this year

As the Chairman has mentioned, BNFL's £299 million loss before taxation in 2003-2004 was largely related to historic issues that are due to transfer next year to the NDA. However, results were disappointing because of continuing difficulties in the Sellafield MOX Plant (SMP) which is taking longer than expected to commission. However, much has been done over the past year in order to deal with the challenges that have arisen during the commissioning of SMP. We are doing everything we can to ensure that our customers are kept fully informed of the progress made. Also costs at Sellafield were higher as a result of regulatory changes, further security costs and additional work on the legacy ponds and silos project. We continue to suffer significant accounting losses at Magnox due to low electricity prices. All this has led to an operating loss in this year's accounts.

Despite these difficulties and the many distractions of preparing for 2005, we've continued to run our businesses to very high standards and our overall operating performance has been excellent. We met or exceeded a number of operating targets

including reprocessing, vitrification and electricity generation. Newly reorganised business reports are the following:

British Nuclear Group

Turnover at British Nuclear Group was up by 7% at £1,721 million while profit before interest and taxation (including contributions from joint ventures) rose by 4% to £186 million. In 2003-2004, the business met nearly all the operational targets set by BNFL ALFA and in many cases did considerably better.

At Sellafield, Magnox spent fuel operations reprocessed more fuel than in 2002-2003 and beat its target for 2003-2004 by 14%. Thorp reprocessing plant achieved its target of shearing over 670 tonnes of fuel for British Energy and customers overseas. The vitrification of our high-level waste has been performing well, with the vitrification lines meeting their increased output targets as planned.

At Magnox, we exceeded our electricity generation target by 5%. Oldbury power station had its best output ever and Sizewell A passed a milestone by generating its one hundred billionth kilowatt hour of electricity. The amount of Magnox spent fuel sent to Sellafield exceeded target by over 13%.

The project to decommission the Windscale Advanced Gas-cooled Reactor is a year ahead of schedule and we've made a strong start on recovering all the intermediate-level waste streams at the Trawsfynydd decommissioning site.

The success of the trials leading to the reduction of the Technetium-99 discharges from Sellafield has been a major technical achievement.

Westinghouse

The work to strengthen customer relationships meant another strong set of results at Westinghouse. Turnover and profit before interest and taxation (after a small loss on sale of fixed assets) were both ahead of target at £1,125 million and £52 million respectively and the company took a record £1.58 billion in new orders.

The year saw more major contracts and the completion of others won in previous years. Among the highlights, the business

completed its second repair and maintenance project at the Qinshan site in China and made its first delivery of fuel to Electricité de France (EDF). In the service sector, EDF named Westinghouse as the leading supplier of steam generator services for the second year running.

Nuclear Sciences and Technology Services (NSTS)

Our research and technology function has been restructured and refocused to create the commercial NSTS division, as well as the Technology Centre helping to preserve Britain's nuclear capability for the future. Turnover for the year was £132 million. The change of name to Nuclear Sciences and Technology Services signals a more commercial and customer focused approach to its activities in meeting the technical needs of the NDA.

Spent Fuel Services (SFS)

SFS increased its turnover by 18% to £107 million and recognised profit of £18 million. The business has had another active year responding to customers' requirements for recycling their spent fuel. The year's highlights included renegotiating contracts to give customers greater cost certainty in the face of pressures arising from deregulated electricity markets. We also made 35 movements of spent fuel from Europe to Sellafield.

BNFL ALFA

In its role of foreshadowing the NDA, BNFL ALFA is responsible for the assets, liabilities and funds that will pass from BNFL to the NDA on 1 April 2005. It is now working with the Department of Trade and Industry's shadow version of the NDA, the Liabilities Management Unit (LMU), to help BNFL to understand the NDA's future requirements. It is setting progressively tougher targets for British Nuclear Group and monitoring its ability to carry out contracts on time, within budget and in a way that maximises performance. The domination of MOX and Magnox issues coupled with higher Sellafield costs and incentive fees to other parts of BNFL meant that ALFA recorded an accounting loss of £545 million before interest and taxation.

Energy Unit

The Energy Unit will look at keeping our nuclear expertise and skills alive should the Government decide to embark on a nuclear rebuilding programme.

Urenco

During 2003-2004, Urenco continued its expansion, increasing its share of the world demand for enrichment services from 15% to 18%. It also entered into an agreement with Areva for the sale of a 50% stake in its newly formed technology subsidiary, Enrichment Technology Company Limited. The transaction is expected to complete in the next financial year, subject to the required governmental and competition clearances being granted. Urenco is also progressing its plans to construct a fourth enrichment plant which will be located in the United States, the licence application is currently being processed.

BNFL's 33% shareholding in Urenco continues to provide the Group with positive returns to both profit and cash flow. During 2003-2004, our share of Urenco's operating profits amounted to £43 million.

Health, safety, security and the environment

While BNFL has always aimed for world class standards of health, safety, security and environmental performance, the new competitive regime makes it even more important to acquit ourselves exceptionally well in all these areas. Our customer, the NDA, will expect nothing less and BNFL will not win contracts unless its standards are exemplary.

The trends this year are very positive. We continued to improve against all of our environmental and safety indicators and exceeded many of our key targets. Our nuclear safety was the best ever and we improved our conventional safety record with lower scores for all our accident frequency rates.

As well as raising our own standards, we're working with the Regulators to make sure that safety and sound practice are firmly embedded in the NDA's system of penalties and incentives for all its contractors.

Building trust

When I joined BNFL last August, I was delighted to find a clear and widely promoted set of values that are consistent with my own views on how this company should be run. Along with being safe and environmentally responsible, these values speak to excelling in our operations, generating value and profit, being committed to the success of our customers and acting with integrity and respect for people.

The last is particularly pertinent. An open and trusting environment is essential for the organisation to work and for people to give of their best. Integrity and respect are also important externally. This is an industry about which people have strong views, both for and against. I see it as part of my job to encourage a free and informed debate. As long as I am Chief Executive, we will try to present the facts of the nuclear industry as simply and transparently as possible so that all shades of opinion – even if they disagree with us – can at least feel they trust us.

As the Chairman has indicated, BNFL has been moving in this direction for a number of years. Last year saw the publication of our first report on corporate social responsibility which went on to win the ACCA (Association of Chartered Certified Accountants) Award for Best First Time Social Reporter in February 2004. The following month we were pleased to be ranked 43rd in the Business in the Community Top 100 Corporate Responsibility Index and in the Top Ten 'Best at Managing Environmental Issues' in the same index. The fact that public trust in BNFL, as measured by MORI, has now returned to pre-1999 levels is an indication of how far we have come in communicating openly and honestly with our stakeholders.

Nuclear power in the future

Looking ahead, I echo the Chairman's view that Britain needs an energy policy and we believe that part of our role is to help protect Britain's nuclear skills base for future generations. Given

the political commitment to reduce carbon emissions and make greater use of non-CO₂ energy sources, we're convinced that nuclear power can make a valuable contribution to the UK's energy mix over the longer term.

In NSTS and our Technology Centre, we have a centre of excellence for keeping BNFL at the forefront of nuclear technology and nurturing the skills that Britain may need in the future. Through Westinghouse, we own the most advanced reactor technology – the AP1000 – while our international research collaborations are helping to develop new generations of reactors. In the UK, our university alliances ensure that more academics are engaged in nuclear research and are helping to attract new talent into the industry. At the same time we are keeping alive the knowledge and skills that will be needed if the Government should decide to embark on a nuclear rebuilding programme.

Prospects

Nearly a year into the job, I'm excited by the prospects. We welcome the chance to operate in the new competitive UK clean-up marketplace and are determined to play our part in helping the NDA achieve its objectives. We believe, furthermore, that BNFL has all the makings of a profitable and growing enterprise. We're ready to compete and have the knowledge, skills and experience to succeed.

Finally, my thanks must go to our retiring Chairman, Hugh Collum. Hugh's influence on the company and the industry has been immense and all of us in BNFL wish him every success in the future.

Mike Parker Group Chief Executive

Highlights of the year

SINCE THE APPOINTMENT OF MIKE PARKER AS GROUP CHIEF EXECUTIVE ON 1 AUGUST 2003, THE HIGHLIGHTS OF THE YEAR INCLUDED:

STRONG OPERATING PERFORMANCE

Strong improvement in operating performance – higher rate of reprocessing and vitrification at Sellafield; 5% increase in electricity generation; major new contracts for Westinghouse.

Safety, security and environmental standards continue to improve with best yet nuclear and environmental safety performance.

CONTINUING IMPROVEMENT IN EHS&Q

BRITISH NUCLEAR GROUP LAUNCHED

Restructuring of the company completed prior to the formation of the NDA in April 2005. British Nuclear Group established as the focus of BNFL's clean-up operations.

BNFL's research and technology function restructured to meet the technical and commercial needs of the NDA.

RESEARCH AND TECHNOLOGY RESTRUCTURED

WESTINGHOUSE SUCCESSES

Westinghouse continues to win important new contracts. Now strongly positioned should the United States and Europe decide to build new nuclear power stations.

Gordon Campbell appointed as new Chairman having been a Non-Executive Director of BNFL since 1 August 2000.

NEW CHAIRMAN APPOINTED

Business review:

British Nuclear Group



- 1 Turbine maintenance at Chapelcross power station.
- 2 Significant progress has been made in the decommissioning and clean-up of Sellafield plants.

LAWRIE HAYNES
Chief Executive, British Nuclear Group

In May 2004, the Government Services Group relaunched itself as British Nuclear Group, to become a specialist clean-up business within BNFL, focused on the clean-up and decommissioning of UK nuclear sites. Its principal aim is to help the UK Government achieve its clean-up programme quickly, safely and cost-effectively – and to do so better than its competitors.

Results

	2003-2004 £m
Profit before interest and taxation	186
Total turnover	1,721
Average number of employees	13,688

Cost efficiencies and the start of a vigorous drive for better operational performance are already showing results in British Nuclear Group's financial performance. Both Environmental Services and BNFL Inc. had their most profitable year ever. By achieving 141 of the 150 key targets set by BNFL ALFA, British Nuclear Group earned a fee of £140 million – an increase of over 3% in both turnover and profit on the previous year.

British Nuclear Group EHS&Q performance

	Sellafield M&O Services	Magnox	Environmental Services	BNFL Inc.
Days Away Case Rate: †#				
2001-2002	0.53*	0.24	0.93	0.41
2002-2003	0.39	0.38	0.30	0.25
2003-2004	0.22	0.12	0.16	0.37

Total Recordable Incidence Rate: †#				
2001-2002	1.11*	0.43	0.93	1.91
2002-2003	0.46	0.43	0.49	1.78
2003-2004	0.25	0.24	0.24	1.15

Organisational structure for 2003.

*Recalculated following formation of Sellafield Management and Operations Services to allow year-to-year comparisons.

†BNFL employees + contractors.

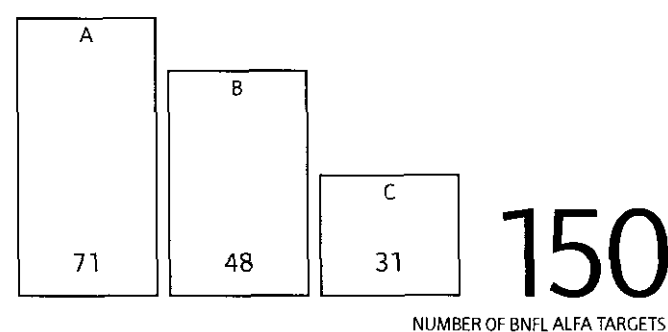
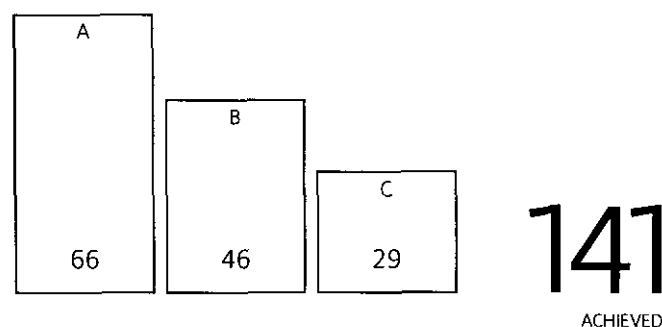
#Rates based on 200,000 hours worked on a 12 month rolling period.

We are determined to keep improving our safety and environmental performance. Our target is zero incidents and the past year has seen excellent progress. Capenhurst, Hunterston A and the Windscale Advanced Gas-cooled Reactor project all achieved exemplary safety records with zero recordable injuries during the year. Hunterston A was one of only four facilities to receive the prestigious 'Scotland's Health at Work' gold accreditation for occupational health. Wylfa and Trawsfynydd also received gold awards from the Welsh Assembly for managing safety at work.

Safety and environmental performance at our operating Magnox power stations was good, remaining well within the key performance measures and showing further improvement. Magnox Generation won the 'Electricity Sector Award' in RoSPA's 2004 health and safety competition; this is based on safety performance over the last five years and is an excellent achievement. However, Dungeness A power station received an enforcement notice relating to errors in sampling of liquid discharges.

BNFL Inc. has one of the best safety records of all large US DoE contractors and received eight awards from the National Safety Council. However, it also received a notice of environmental violation from the Idaho Department of Environmental Quality for a number of minor incidents that have since been corrected.

BRITISH NUCLEAR GROUP PERFORMANCE AGAINST BNFL ALFA TARGETS



NUMBER OF BNFL ALFA TARGETS

- A SELLAFIELD M&O SERVICES
- B ENVIRONMENTAL SERVICES
- C MAGNOX

ALFA TARGETS APPLY TO UK OPERATIONS ONLY

- 1 The Thorp plant at Sellafield sheared 671 tonnes of fuel in 2004.
- 2 Decommissioning of the Windscale AGR is a year ahead of schedule.

Electricity generation target exceeded by

5%

Magnox generated 6% of the UK's electricity in 2004

Reprocessing and vitrification targets exceeded

Operational performance

The market we are about to enter will require us to progressively improve our operational performance and only by achieving real improvement will we be able to earn incentives from the newly formed NDA. Targets previously set by BNFL ALFA have already improved operational and financial performance across our business, those for 2004-2005 are even more challenging.

Three year operating performance

	2001-2002	2002-2003	2003-2004
Vitrification plant containers to store	120	333	341
Thorp tonnes sheared	736	502	671
Magnox tonnes decanned	786	765	1,038
Electricity output TWh	16.8	17.6	16.6

Project success: Magnox reprocessing at Sellafield

Magnox reprocessing celebrated this year after reprocessing over 1,000te of spent fuel including 125te of legacy fuel, a notoriously difficult type to reprocess. With the announced closure dates of the UK's Magnox power station fleet, hitting our reprocessing targets is essential if the declared dates are to be achieved in time for the closure of the Magnox reprocessing plant by 2012.

Project success: Magnox electricity generation

At Magnox, we generated 5% more electricity than our target due to the continued good performance from Dungeness A, Sizewell A, Wylfa and Oldbury. This impressive performance is due to investment in improvement projects which have delivered reduced outage duration. We have also applied techniques developed for planned outages to reduce the impact of unplanned losses.

During the year Sizewell A generated its one hundred billionth kilowatt hour of electricity since it started up in 1966 – enough electricity to meet the needs of the whole of England and Wales for about six months.

Oldbury power station had its best year ever with an output of 3.7 terrawatt hours.

We beat our target for sending spent fuel to Sellafield by around 13% and reached our threshold for despatches of fuel from power stations coming off line. Despite the slow start after the closure of Bradwell power station in 2002 we are now on track to meet our revised, but later, target defuelling date.

Alongside these operational successes, however, a number of targets have yet to be achieved specifically at the Sellafield MOX Plant. Commissioning at SMP has been slower than anticipated, however a significant amount of work is underway to resolve production issues. Elsewhere, a project to remove redundant pipes under the Irish Sea was delayed because of technical and weather problems and a contract to construct a putrescent waste disposal facility has been terminated, following an incident. The project remains on hold, pending an internal inquiry.

Decommissioning and clean-up capabilities

With decommissioning successfully completed at two UK research reactors – the Scottish Universities Research Reactor near Glasgow and the ICI Triga Mk 1 Reactor at Billingham – we have continued to strengthen our reputation for solving complex decommissioning problems.

Project success: Windscale AGR

The Windscale Advanced Gas-cooled Reactor (WAGR) decommissioning project is a year ahead of schedule. We demonstrated our ability to provide innovative tailored solutions by using hot gas cutting methods to decommission a commercial

sized gas-cooled reactor. This transferable technology enabled faster and more economical decommissioning of the vessel and delivery of waste in an easy to handle form.

BNFL Inc. has made good progress on a range of environmental clean-up contracts in the United States. Two contracts have dominated: East Tennessee Technology Park (ETTP) and the operation of the Advanced Mixed Waste Treatment Plant (AMWTP) in Idaho. Both projects have continued to perform to the targets established last year. The coming year will see the completion of operations at ETTP and the start of waste shipments from AMWTP.

Working with our stakeholders

British Nuclear Group places great importance on winning and keeping the confidence of its stakeholders. Thanks in part to our good relationships with local communities, we gained the intermediate-level waste safestore planning consent at Trawsfynydd from the Welsh Assembly and the 'Consent to Decommission' at both Hinkley Point A and Bradwell power stations from the Nuclear Installations Inspectorate. This is a landmark, permission granted for the first time to decommission nuclear power stations under new legislation introduced in 1999.

Preparing for 2005

As well as carrying out its existing activities, British Nuclear Group has been working hard to be ready for its new role as a supplier of clean-up services to the NDA. A strong and experienced management team has been put in place to drive the necessary changes – instilling greater commercial acumen, tightening financial controls, developing consistent policies and procedures, integrating processes and systems across the business and in every way preparing the company for the new, competitive marketplace. Although much remains to be done, the team has made excellent progress during the year.

Business review:

Westinghouse

Record new orders of
£1,580m

£1,125m
turnover
in 2004

STEPHEN TRITCH
Chief Executive, Westinghouse

Westinghouse provides fuel, services, technology, plant design and equipment to the worldwide nuclear electricity industry. Its main goal is to help customers produce safe, low-cost, reliable and environmentally friendly electricity. Nearly half the nuclear power plants in operation around the world use Westinghouse technology.

Results

A worldwide resurgence of interest in nuclear power and further efforts to strengthen customer relationships helped Westinghouse to another impressive set of results. In 2003-2004, the company exceeded its targets for turnover, cash flow and profitability while logging a record £1.58 billion in new orders.

2003-2004
£m

Turnover	1,125
Profit before interest and taxation:	
Before amortisation of goodwill*	93
After amortisation of goodwill*	52
Orders entered	1,580
Average number of employees	7,665

*Profits stated in the table above include a small loss on the sale of fixed assets of £2 million.

Worldwide worker safety
performance improved by
28%

- 1 In the United States, Westinghouse entered into a comprehensive alliance-type relationship with Constellation Generation Group, operator of a fleet of nuclear power plants including Nine Mile Point in New York.
- 2 Westinghouse continues to move nuclear technology forward with development of advanced technologies like the AP1000.
- 3 Westinghouse continues to develop a strong fuel manufacturing business serving nuclear plant operators throughout the world.
- 4 In China, Westinghouse completed a major reactor vessel nozzle project ahead of schedule at the Qinshan site.

Safety

While achieving these results, Westinghouse also improved its worldwide objective for worker safety by 28%. At the now-closed fuel fabrication facility in Hematite, Missouri, where a decontamination and decommissioning project is under way, Westinghouse has completed two consecutive years without a single recordable accident.

Contracts

During the year, Westinghouse gained more major contracts while fulfilling a series of landmark contracts achieved in previous years. The completion of the Qinshan Phase II, Unit 2 reactor vessel nozzle project ahead of schedule marked the second successful repair and maintenance operation at this Chinese site in the last three years. In addition, Westinghouse made its first delivery of nuclear fuel to EDF—a major breakthrough in an important market. In the service sector, EDF ranked Westinghouse as France's number one supplier of inspection, maintenance and other steam generator services for the second consecutive year.

Westinghouse has three main business units:

Nuclear services

PROVIDES MAINTENANCE AND REPAIR SERVICES INCLUDING EQUIPMENT AND ENGINEERING FOR CUSTOMERS OPERATING NUCLEAR PLANTS.

Nuclear fuel

PRODUCES FUEL PRODUCTS, MATERIALS AND COMPONENTS, AS WELL AS SERVICES, AND TECHNOLOGY FOR CUSTOMERS OPERATING PWRs, BWRs, VVERs, AGRs, AND MAGNOX REACTORS.

Nuclear power plants

OFFERS PLANT DESIGN EXPERTISE, EQUIPMENT, AND COMPONENT MANUFACTURING FOR CURRENT AND FUTURE GENERATIONS OF NUCLEAR POWER PLANTS.

The AP1000 – the Westinghouse design that is widely hailed as the world's most advanced nuclear power plant – received its draft safety evaluation report from the US Nuclear Regulatory Commission (NRC) in June 2003. It is also on schedule to receive final design approval from the NRC in 2004. As a result, Westinghouse is well placed for new plant projects in the United States where the government publicly supports the construction of at least one new plant by 2010.

Westinghouse will bid the AP1000, as China is expected to issue a tender offer for its next generation of nuclear power plants soon.

Servicing existing plants

While the resurgence of the new plant segment provides exciting opportunities, Westinghouse's success depends on its ability to keep providing replacement fuel along with maintenance and other services at a quality and cost that will help make the existing fleet of nuclear plants even more competitive with plants based on fossil fuels.

To this end, Westinghouse continues to strengthen its customer relationships. Notable during the year was the company's strategic alliance with Constellation Generation Group that gives Westinghouse the opportunity to contribute to, and be rewarded for, improvements in operating efficiency in the Constellation fleet.

Also during the year, Westinghouse won a number of traditional fuel and service contracts, including:

- A three-year award from TVO in Finland to provide boiling water reactor (BWR) fuel to the Olkiluoto 2 nuclear power plant.
- A contract from Nuclear Management Company to replace five reactor vessel heads at plants in the Upper Midwest of the United States.
- A sole-source award to provide replacement parts and services to Pacific Gas & Electric's Diablo Canyon nuclear power plant.

New plants

With more countries now taking the decision to build new nuclear power stations, Westinghouse has strengthened its presence in this segment.

More than 30 nuclear power plants are currently under construction around the world, most are in Asia where Westinghouse is active in South Korea's vigorous new plant programme. In the United States, seven major plant operators joined Westinghouse and General Electric in March 2004 in forming a consortium to work with the US DoE. The aim is to demonstrate and test a new licensing process for obtaining a combined construction and operating licence of the kind required to build advanced nuclear power reactors in the United States.

Investments

With support from BNFL, Westinghouse made a number of investments to improve its future financial performance and maintain its market leadership. The main investments were:

- The formalisation of the company's minority stake (24.5%) in the LES partnership, a consortium of Westinghouse, Urenco and key utilities that intends to build an advanced uranium enrichment facility in the United States.
- An announcement of intent to acquire a controlling interest in PaR Nuclear, a leading provider of new equipment and maintenance services for refuelling systems and reactor containment and spent fuel building cranes.
- A teaming agreement with Master-Lee Energy Services that enhances Westinghouse's ability to provide refuelling and reactor coolant pump and motor services.
- Expansion of the company's fuel fabrication facility in Columbia, South Carolina to accommodate the production of BWR fuel to complement the wide range of pressurised water reactor (PWR) fuels already manufactured there.

Customer relationships

To provide even better service to customers around the world, Westinghouse has initiated a process improvement programme called 'Customer 1st'. This aims to improve the company's operations while making it easier for customers to do business with

Westinghouse. A Customer Advisory Board consisting of 11 top nuclear utility executives from Europe, Asia and the United States will ensure that 'Customer 1st' maintains its focus and that Westinghouse continues to provide the highest quality products and services in a manner that totally fulfils the needs of its customers.

The next generation

The revitalisation of the worldwide nuclear power industry has had a positive effect on public perception, particularly among the young who are now showing greater enthusiasm for a career in the industry. To encourage this interest, Westinghouse has expanded its college intern and recruitment programmes and has, over the last five years, hired more than 300 young engineers and technologists direct from university. This contrasts with virtually no recruitment of young people through much of the 1990s. The programme will accelerate as demand for nuclear power increases as existing plants extend their licences and new plants are built.

Preparing for 2005

As part of the restructuring of the UK nuclear industry, from 1 April 2005 ownership of Westinghouse's UK nuclear fuel operations at the BNFL Springfields site will transfer to the NDA. Westinghouse will continue to manage and operate the site under an M&O arrangement with the NDA. As a consequence, income to Westinghouse will be in the form of a management fee commensurate with the level of risk assumed by a management contractor.

Business review:

Nuclear Sciences and Technology Services

PETER BLEASDALE
Chief Executive, Nuclear Sciences and Technology Services

NSTS is a new business group that has come out of our reorganised R&T function to serve the NDA and other external customers. It will provide nuclear research, development and scientific services on a commercial basis.

Following the restructuring of the industry in 2005, NSTS will provide support to the NDA, site licence companies and other customers. NSTS is also engaged in the promotion of nuclear research and development in academic institutions across the country.

Results

NSTS turnover for the year was £132 million. Products and services supplied to BNFL customers amounted to £123 million, including £28 million for work carried out on the new BNFL Technology Centre on behalf of BNFL ALFA. Sales to external customers, including British Energy and the Ministry of Defence, totalled £9 million.

Due to changes in BNFL's customer programmes, anticipated income fell during the year by £10 million. NSTS managed this reduction to ensure no adverse effect on the overall financial results of BNFL or NSTS.

- 1 The BNFL Technology Centre at Sellafield, a centre of excellence for research and technology.
- 2 A robot manipulator developed by BNFL to work in radioactive environments.

	2003-2004 £m
Turnover	132
Profit before interest and taxation	7
Average number of employees	910

NSTS numbers are included in the corporate business segment in the Notes to the accounts.

Safety

During the year, excellent safety performance was achieved with NSTS's OSHA rates the best since 1998 and behavioural safety observations significantly increased. NSTS also won a highly prestigious RoSPA Sector Award, which reflected commitment to safety. The award took account of excellent overall performance and supporting initiatives such as safety leadership, behavioural safety, operational experience feedback and other projects driving the development of a safe operating environment.

Preparing for 2005

NSTS has been preparing for the restructuring of the nuclear industry in the UK. NSTS will become a fully owned BNFL subsidiary from 1 April 2005. This signals a transformation for NSTS and a separation from the Group Technology function.

Responding to Government requirements, NSTS will seek to establish long-term stability and sustainability as a national capability, contributing to nuclear liability cost reductions while achieving reasonable income and profit margins.

The overriding objective of NSTS's transformation plan is to create a 'customer focused and business aware' operating culture. Management and business processes have already been strengthened and streamlined.

In finalising the organisational structure of NSTS, the decision has been taken to transfer the Safety and Environmental Risk Management (S&ERM) function to British Nuclear Group.

A challenging and successful year for NSTS has provided many insights into the new competitive environment. Building on its successful record, NSTS is well placed to succeed as a customer focused, nuclear sciences and technology services provider. Its future development will continue to be guided by the needs of its customers, Regulator, Shareholder and other stakeholders.

Contracts

In preparation for its trading subsidiary role, NSTS has been operating as a supplier to BNFL ALFA as it shadows the future role of the NDA. This arrangement will continue during 2004-2005.

Under formal agreements with ALFA and British Nuclear Group, NSTS has met rigorous cost control and effectiveness targets and a range of other demands for products and services. These included technical support to improve the management of existing facilities, site remediation activities and other initiatives such as the University Research Alliances that are leading a revival in the study of nuclear sciences.

NSTS

CREATES A COMMERCIAL FOCUS
FOR RESEARCH AND TECHNOLOGY

Business review:

Spent Fuel Services

DAVID BONSER
Director, Spent Fuel Services

SFS acts as the point of contact for utility customers in the UK and overseas that send used fuel to Sellafield for recycling. It handles sales and contracts, dealing both with utilities and with Management Services Sellafield (operator of the reprocessing and MOX plants) to ensure that customers' requirements are met. It also provides a rail and sea transport service, primarily for bringing spent fuel to the reprocessing plants and returning MOX fuel to customers.

Results

	2003-2004 £m
Turnover	107
Profit before interest and taxation	18
Average number of employees	494

Ahead of the formation of the NDA, the customer liaison side of SFS has operated according to an agency agreement whereby SFS is paid a retainer and incentive fee related to the value it generates for the site owner – currently BNFL ALFA but eventually to be the NDA. This arrangement made a positive contribution to earnings in 2003-2004.

- 1 Fuel for reprocessing at Sellafield is unloaded at Barrow.
- 2 BNFL's European fuel transport ship Atlantic Osprey.

On the transport side, SFS has retained ownership of its various operations – the UK rail subsidiary, Direct Rail Services (DRS), and the marine service, International Transport. Despite a good performance in the UK and by the Japanese business, the SFS European business once again made an overall loss, mainly as a result of low volumes and high fixed costs.

Safety and quality

During the year, safety performance has continued to show improvements with a Total Recordable Incidence Rate (TRIR) below 0.6. DRS maintained its good safety record and, for a further year, recorded no signals passed at danger.

For the first time this year, SFS as a whole gained ISO 9001 quality certification and ISO 14001 environmental certification for its company-wide management systems. It also retained other approvals for its subsidiaries.

Operational highlights

We continue to respond to our customers' requirements for recycling spent fuel, recovering the uranium and plutonium, treating the residual waste and either returning or disposing of it at Sellafield. We revised contracts with a number of customers to offer them greater certainty as to the long-term costs of such services. We also contributed to the Government consultation on proposals to allow overseas customers to accept smaller volumes of high-level waste in place of greater volumes of low and intermediate-level waste – a move designed to cut the number of shipments.

Although the Sellafield MOX Plant (SMP) had a disappointing year with slower than expected progress in its commissioning, fuel assembly manufacturing has been successfully demonstrated and we are on track to implement measures that ensure we meet Japanese fuel manufacturing quality requirements and have gained approval for SMP to manufacture pellets and rods for European PWR fuel.

The past year saw the completion of 35 movements of spent fuel from Europe to Sellafield. In order to provide a secure route for future returns of waste to the Continent, we have re-sited our Dunkirk terminal and used it successfully since September

2003. Our international shipping subsidiary, PNTL, completed two further voyages from France to Japan as part of the waste return programme. The rail business in the UK had a record year with around 900 flask movements and a growing volume of non-nuclear, commercial traffic.

We have also been reviewing and upgrading the assets within the business. DRS has introduced ten new Class 66 locomotives and fitted the mandatory train protection warning system (TPWS) to all its other locomotives. We have also begun investigating a new, more efficient design of MOX ship with a view to replacing existing vessels in due course.

We continued to support the commissioning of a new reprocessing plant at Rokkasho in Japan. We also undertook studies and offered assistance to utilities in Ukraine, China, South Korea and France on various aspects of design, development and the licensing of proven nuclear technology from the UK.

Preparing for 2005

Finally, we contributed to the debate on establishing an effective service arrangement for our new customer, the NDA. While the business model is still evolving and there is more work to be done, it is clear that SFS will act as the hub of a triangular relationship between the NDA, Management Services Sellafield and our various utility customers. The necessary legal, contractual and organisational arrangements will continue to be developed ahead of the expected transfer on 1 April 2005.

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EUROPEAN FUEL MOVEMENTS
COMPLETED IN 2004

BNFL ALFA

DAVID BONSER
Director, BNFL ALFA

The aims of BNFL ALFA are to drive change in BNFL by being a consistently demanding and challenging internal customer while performing exceptionally well as a safe, secure, environmentally responsible and cost-effective liabilities manager.

A crucial role

For the last two years, BNFL ALFA has had responsibility for all the BNFL assets, liabilities and funding that we expect to pass to the NDA on 1 April 2005.

BNFL ALFA drives change in BNFL by acting as a consistently demanding and challenging customer within the BNFL internal market. In close partnership with the Department of Trade and Industry's LMU, BNFL ALFA is helping the Company to understand the future requirements of the NDA and to perform according to the demands that are likely to be placed upon it. This ensures that British Nuclear Group, Spent Fuel Services, Nuclear Sciences and Technology Services and Westinghouse – Springfields are ready to compete for contracts to manage and operate the assets once they have passed to the NDA.

In the run up to this financial year, BNFL ALFA placed internal contracts for 2003-2004 for the management and operation of BNFL ALFA's assets. These contracts contained a strong focus on meeting targets safely, securely and in a way which protects the environment as well as meeting operational and project targets that required higher performance against the LMU's requirements for programme management.

Contractors are also incentivised to manage BNFL ALFA's income streams – such as electricity generation and Thorp operations – and to keep costs within targeted amounts. The contractors' performance against all targets is regularly reviewed and challenged by BNFL ALFA and the LMU.

Results

	2003-2004 £m
Turnover	1,449
Loss before interest and taxation*	545
Average number of employees	32

* The loss stated above includes a small profit of £6 million on the sale of fixed assets.

Turnover increased to £1,449 million (2003: £1,373 million) and the loss before interest and taxation is £545 million (2003: £358 million before operating exceptional items). This reflects challenges such as the performance of Sellafield MOX Plant, additional Sellafield costs and falls in the market price of electricity.

Contractor performance during the year

Sellafield Management and Operations Services

Performance against many targets has been ranked as 'excellent'. Much effort has been devoted to formulating arrangements for programme management in conjunction with the LMU. Life Cycle Baseline Plans (LCBLs) and Near Term Work Plans (NTWPs) have been created, together with supporting systems and procedures. The Sellafield and Drigg NTWPs scored among the highest in the country and were deemed to be an example of best-in-class.

Operational activities have continued to improve with both Thorp and Magnox Reprocessing plants performing very well. Magnox Reprocessing exceeded 1,000tes for the first time in eight years. Processing of legacy fuel in the Sellafield Fuel Handling Plant resulted in a lowering of stocks from 610tes to 485tes, a significant contribution to hazard reduction. Vitrification of high-level waste and storage of vitrified product has progressed well and delivered real reductions in hazard. The success of the TPP trials to remove Technetium-99 are the culmination of several years of multi-disciplinary work.

Strategies for 'safer, faster, cheaper' remediation, with particular emphasis on older and redundant ponds and silos, have been developed. The removal of the plutonium contaminated materials (PCM) inventory from Drigg site and aged on-site stores to new,

purpose-built PCM stores has progressed well and a further PCM store is scheduled to be completed on target. These activities reduce hazard relating to the storage of intermediate-level waste.

Work is underway to start improving the performance of the MOX plant which is still not performing as scheduled.

Reactor operations contract

The key features of this year's contract performance were beating the target for generation output, exceeding plan for the transfer of spent fuel and further decommissioning work while also improving safety and environmental performance.

The reactor operations contract covers the whole lifecycle of reactor activities from generation through defuelling to decommissioning at the reactor sites run by Magnox Generation and includes early decommissioning work by Environmental Services. During the year, the Nuclear Installations Inspectorate granted permission for the decommissioning programme at both Hinkley and Bradwell, a significant step in preparing the way for cleaning up these reactor sites.

Decommissioning contracts

Environmental Services has managed the decommissioning programme on four sites – Berkeley, Capenhurst, Hunterston and Trawsfynydd. Safety standards have remained high with, for example, Hunterston into a third year without a lost-time accident. Contract targets have been met across a broad front, the main requirements being the recovery of waste streams at all the sites. Visible progress has been made at Trawsfynydd with the demolition of the turbine hall. The overall decommissioning project at the site can now proceed with confidence following planning approval to construct an intermediate-level waste store and to convert the reactor buildings into safestore structures.

Spent Fuel Services

The contractual requirements placed on SFS by BNFL ALFA were designed to ensure excellent delivery for utility customers and value for BNFL.

Progress on arrangements for waste returns, strategic scenario analysis and support for NTWPs and LCBLs has begun to create

an organisation that focuses on LMU/NDA requirements. In all parts of the business, including International Transport, it is now developing activities that will support NDA contracts.

Nuclear Sciences and Technology Services

Working with NSTS, BNFL ALFA has developed a programme of work that satisfies near-term site needs while also maintaining the levels of technical excellence that are vital to underpin the UK's nuclear programme over the longer-term.

Preparing for 2005

In the final year before the establishment of the NDA, BNFL ALFA has in place contracts which replicate the contracts we expect the NDA to award. This has been achieved by working closely with the LMU and the UK's Regulators in preparing contracts and identifying the areas for incentivisation.

The overall focus of BNFL ALFA's final year will be to act as closely as possible as we expect the NDA to act and, through our contracts, to concentrate on implementing change in BNFL and being an innovative liabilities manager. We will also work closely with the DTI, Regulators and the emerging NDA to ensure a successful transition to the new regime.

BNFL ALFA

IMPLEMENTING CHANGE AND
IMPROVING PERFORMANCE

Commercial and social responsibilities

Our goal is to be an economically viable, environmentally responsible and socially beneficial company that is fully accountable for its performance.

Corporate Social Responsibility

We recognise that we cannot succeed financially without also protecting the environment and contributing to the good of society. Corporate Social Responsibility (CSR) is about meeting our responsibilities in all these areas. It underpins the way we do business and is part of our values and principles.

Managing CSR

The year has seen further developments in the way we manage our CSR activities. At the top level, CSR will be the responsibility of the Environment, Health and Safety (EH&S) Board Committee. In addition, our Chief Executive, Mike Parker, leads an Executive Group on CSR that meets at least twice a year. Westinghouse and British Nuclear Group now have strategies for handling CSR within their own businesses.

Stakeholder dialogue

The BNFL National Stakeholder Dialogue, established in 1998, will come to an end in October 2004. Intended to inform BNFL's decision-making on environmental issues, this successful initiative has led to a series of independent reports by stakeholder working groups on issues such as waste management, plutonium and security.

The Dialogue has also looked at social and economic issues affecting the company, resulting in a number of economic studies on the impact of Sellafield on West Cumbria. The process has also helped to inform the DTI on the setting up of the NDA.

BNFL in the community

Every business has an impact on the society in which it operates. At BNFL we recognise our responsibility to make a positive difference, to treat our neighbours with respect, to earn society's trust and to demonstrate our commitment to local communities.

Education

BNFL is committed to supporting national, regional and local education schemes at all levels.

Through the Engineering Education Scheme, we support a number of projects to develop the skills of young people. Sixth formers are offered hands-on experience in solving real engineering problems leading to a better understanding of engineering as a profession.

Our Yottenfews environmental education project provides an outdoor learning resource for schools and other groups. Based at the Sellafield Visitors' Centre children can experience wildlife habitats and activities such as pond dipping.

In the US, Westinghouse supports an 'in-roads' programme that promotes the development and education of college students through training and placements. BNFL Inc. has supported the Teacher of the Year awards which recognise excellence among teachers and the important role they play.

- 1 BNFL routinely monitors the environment around its plants.
- 2 Engineers of the future participate in BNFL's young engineers scheme.
- 3 David Bonser collects the ACCA Sustainability Reporting Award 2003 from Baroness Young.

Through the Magnox Business, our partnership with the Association for Science Education continues to develop. Last year over 200 schools took part in the Association's Science Challenge competition.

Community investment

We continue to invest in and be involved with, the communities near our sites. Our community investment policy focuses on areas where we believe we can add the most value and often tackles difficult social issues.

In partnership with the Whitehaven Community Trust in West Cumbria, we have helped to create a hostel for homeless young people. Its contribution supports the Government's drive to tackle social exclusion.

In Sweden, we work in partnership with the community to support education and sports activities that benefit both the business and local people.

We support the Foyer Federation, one of the UK's leading youth organisations. The Workbank project helps to formulate a personal action plan for ten young disadvantaged residents, enabling them to build the skills to move forward into further training or employment.

Employee involvement

We actively support those members of our workforce who volunteer their time and commitment in helping others.

Employees in the UK and the US who contribute outstanding personal service to their communities receive recognition in the form of a grant for their nominated charity. Our Community Service Award scheme enables employees to develop their voluntary activities in areas such as community fundraising and recreational programmes.

Through mentoring, facilitation and teambuilding activities, our employees continue to support 'businessdynamics' a UK charity that aims to bring business to life for young people.

In the US, Westinghouse co-ordinates the Rube Goldberg Contest that encourages high school students in engineering to transform everyday material into innovative machines. Over 50 engineers contribute to the annual competition as mentors, judges and volunteers.

Economic regeneration

We recognise that our licence to operate depends upon our ability to ensure the trust and support of the communities in which we operate. For this reason, we aim to play our part in creating self-sustainable communities and increasing the prosperity of local regions. As part of this effort, we support and encourage individuals and businesses in developing the skills to manage their own future.

- 1 School children participate in classroom activities at Sellafield visitors centre.
- 2 BNFL has established strong academic links through its university research alliances in the UK.
- 3 Westinghouse employees in Columbia, USA donate their time and dollars in supporting the local community.

Our partnership with the West Cumbrian Development Fund (WCDF) supports the balanced economic regeneration of West Cumbria. This work builds on the 'Big Tick' award we received last year from Business in the Community. It has been further reinforced by a recent tri-party agreement with Lancaster University Management School, BNFL and WCDF to commission an action programme on the theme of social entrepreneurship in West Cumbria.

Business in the Community survey

This is the second year that we have taken part in Business in the Community's Corporate Responsibility Index and we were pleased to be ranked 43rd in the 'Top 100 Companies that Count'. Our overall score improved from last year and we aim to continue this improvement with the help of feedback from Business in the Community.

ACCA award

Published in 2003, our first CSR Report was well received and gained the 'Best First Time Social Reporter' award in the Association of Chartered Certified Accountants (ACCA) Sustainability Reporting Awards 2003. This success endorses our determination to communicate with our stakeholders in an open and transparent way. The judges commented on the fact that we had directly addressed some major concerns and had not shied away from delicate issues. We aim to build on this success in our next CSR Report.

Environment, health, safety and quality

Nothing is more important to BNFL than the health and safety of its workforce, contractors and the public and the protection of the environment. We are rightly expected to maintain high standards and we take our responsibilities extremely seriously. We also recognise that being safe and environmentally responsible is not only a moral duty, but an integral part of good business and essential to generating value and profit.

We have made enormous strides over recent years in improving our environment, health, safety and quality (EHS&Q) record. For BNFL, regulatory standards are the minimum level of performance and our target is excellence in all areas of our operations. We therefore review our performance every year and constantly seek ways to do better in the future.

This year's performance

During 2003-2004 we continued to improve against most of our environment and safety indicators and achieved all four of our key company targets.

Our nuclear safety performance continued to improve dramatically with the number of events categorised as 'anomalies' on the International Nuclear Event Scale (these being the lowest level of incident) falling to five. There have now been no events at higher levels on the scale for three years.

Our aim is to continue to be safe and environmentally responsible.

We have maintained our stringent controls over the amount of radiation to which our workers are exposed. As in previous years, all our employees received less than the relevant national regulatory limits – in most cases, significantly less. In 2003 our average radiological dose for all classified employees and workers supplied by agencies was 0.87 mSv.

In February 2004, the Committee on Medical Aspects of Radiation in the Environment published a report re-examining data from ten studies conducted over the last 15 years to determine whether radiation exposure on the part of parents can affect unborn children with outcomes such as miscarriages or stillbirths. The report found little evidence linking adverse outcomes to parental exposure. The only human studies suggesting effects were conducted on two groups of workers who received higher radiation doses than workers experience today and are not corroborated by similar findings from other studies or other sites.

We have also improved our conventional safety as shown by the accident frequency rates of our employees and agency workers. We surpassed our Days Away Case Rate target of no more than 0.34 per 200,000 hours worked with a year end figure of 0.27 while our Total Recordable Incidence Rate fell to 0.65 per 200,000 hours worked compared to 0.89 last year. We also achieved our (UK-only) target for reportable 'Dangerous Occurrences'. These are non-nuclear related and cover a range of events such as failures of lifting equipment.

BNFL is highly regulated and subject to a wide range of environmental and safety requirements. There is, therefore, the potential for non-compliance if excellence is not continuously maintained. Regrettably, we were prosecuted twice in 2003-2004 for conventional safety events in the previous year. We also received two statutory notices from the Health and Safety Executive in the UK and three Notices of Violation in the US.

In the UK we maintained most of last year's major reduction in the number of non-compliances with environmental discharge authorisation limits and conditions. This year, there were only four, none of which had a significant effect on the environment. We also received an enforcement notice relating to errors in the sampling of liquid discharges from Dungeness A power station. We are however committed to further improving our performance to achieve our ultimate aim of no non-compliances. While four non-compliances was a slight increase on last year's two, it remains a major improvement on the 14 of the previous year.

Certifications and awards

All our UK nuclear sites and our Västervik fuel fabrication plant in Sweden have retained their certifications to the ISO 14001 International Standard for Environmental Management, as has our International Transport operation. Our DRS subsidiary gained certification to this standard for the first time.

For a number of years we have taken part in Business in the Environment's Index of Corporate Environmental Engagement and Corporate Responsibility Index. This year we improved our performance on both indices and were listed in the Top Ten companies for managing environmental issues.

Our safety performance has also been recognised externally with 20 awards from the Royal Society for the Prevention of Accidents including the electricity and research and development awards for best performance in those sectors. In the US, we have retained three Star Awards under the Voluntary Protection Programme. Approval into the programme is official recognition of the outstanding efforts of employers and employees who have achieved exemplary occupational safety and health.

More information on our EHS&Q performance will be available in our CSR report to be published this autumn.

The quest for constant improvement

BNFL has placed considerable emphasis on improving its EHS&Q culture. Here we have recognised four areas in which we need to keep improving – leadership in EHS&Q, better communications, promoting learning and involving all our people as much as possible. This work has been proceeding with the support and encouragement of our employees and their representatives.

Our programme of behavioural observation, under which people take time to work directly with others to reinforce good practice and improve performance, has been extended into new areas. A large proportion of our workforce is now actively involved in this programme in several parts of the company.

Learning from experience is also vital if the pace of improvement is to be maintained. To this end, BNFL sites share experience with many outside companies and organisations. The aim of these links is to draw lessons from specific events within and outside the company even from those unrelated to the nuclear industry – a recent example being a review of the organisational lessons from the tragic Columbia Shuttle disaster.

As part of its liaison with other organisations, BNFL Inc. recently hosted a meeting of the Department of Energy's Society for Effective Lessons Learned Sharing in Denver, USA.

Preparing for 2005

BNFL's new structure and the formation of the NDA have important implications for the company's EHS&Q performance. High standards will be vital in meeting the needs of our customers and in helping British Nuclear Group to become the NDA's supplier of choice.

Key performance indicators

	Target	Outcome	Achieved
Days Away Case Rate for BNFL employees and agency-supplied workers (per 200,000 hours worked) (Global measure)	≤0.34	0.27	✓
International Nuclear Event Scale Level 1 Events (anomalies) (Global measure)	≤18	5	✓
Dangerous Occurrences (UK only) (As defined in the Reporting of Injuries, Diseases and Dangerous Occurrences Regulations and the Electricity Safety, Quality and Continuity Regulations)	≤15	11	✓
Non-compliance with environmental discharge authorisation limits and conditions (UK only)	≤11	4	✓

Some of the above targets cover our UK operations only because they relate to specific UK regulatory definitions.

LEADERSHIP TEAMS ARE PREPARING FOR THE COMPETITIVE MARKETPLACE

To assure our Chief Executive and our Regulators that the company's new structure will continue to support the highest EHS&Q standards, BNFL has formed a company-level safety committee which is broadly equivalent to the nuclear safety committees covering our sites' activities. This will scrutinise key organisational changes that may have an impact on EHS&Q and will monitor their implementation.

As well as constantly seeking to improve our own EHS&Q standards, we are working with our Regulators to make sure that the NDA's system of penalties and incentives encourages high EHS&Q standards among all its contractors. We are also seeking to clarify and simplify the way we interact with our EHS&Q Regulators to improve our working relationships and ensure we meet their requirements more effectively.

Our people

The creation of British Nuclear Group as a commercial organisation in a competitive marketplace presents new challenges for BNFL. In particular, we need to combine new commercial and customer management skills with our technical and operational expertise and high standards of safety, security and environmental management.

In response to the challenges, we have, over the last year, undertaken a major leadership review in the UK to help prepare our leadership teams for the new competitive marketplace. We have identified skill gaps and brought in new skills, particularly to improve our commercial cutting edge.

We aim to be an employer of choice for high-calibre graduates in commercial, engineering and scientific disciplines. We are proud that our long-term commitment to graduate recruitment and development has again been recognised in our position as a 'Times Top 100 Graduate Employer'. Our comprehensive two-year graduate development programme ensures that all our graduates have the technical, commercial and leadership skills they need to launch their careers. The technical element of this programme is accredited by many relevant institutes. We also encourage all employees to continue their development by joining appropriate professional institutes.

To accelerate the careers of talented individuals, we have also introduced a company-wide three-year leadership development programme for a small number of high-potential graduate managers.

We continue to invest in development opportunities at all levels to improve our business and technical skills. In this context, we have joined the Cogent Sector Skills Council to demonstrate our commitment to maintaining and developing the nuclear skills base in the UK.

In the United States Westinghouse has expanded its intern and recruitment programme and has hired more than 300 young engineers and technologists directly from University.

Financial review

JOHN EDWARDS
Group Finance Director

Overview

Two years ago we recognised the NDA concept in the structure of our internal organisation by the creation of BNFL ALFA and this was reflected both through the presentation of our financial performance and also in the way our UK businesses interacted and were incentivised. In this last financial year, the strategy review and subsequent work have further developed the business model for the post-NDA Group. This, together with the evolution of the NDA structure has resulted in further structural changes. With 12 months to go we can anticipate most of the further changes and the financial profile of the post-NDA Group is now beginning to emerge.

Apart from MOX fuel production at Sellafield where we continue to face challenges in getting the plant running, the underlying operational performance has again been good with all major operational targets being met. Using the new post-NDA business model the Group would have produced an operating result broadly consistent with 2002-2003. This result has, however, been overshadowed by increased accounting losses on our MOX plant, increases in the Sellafield cost base (additional work on legacy ponds and silos project, regulatory changes and extra security costs) and continuing three figure losses on electricity generation. Overall as a result the Group's operating loss at £351 million is worse than last year (£190 million loss before exceptionals).

Our cash position has been adversely impacted by the full year effect of the British Energy (BE) payment standstill which affected the latter part of 2002-2003. Despite this we have financed £510 million expenditure on liabilities from our other cash resources without drawing down from the Nuclear Liabilities Investment Portfolio (NLIP), which has now increased to over £4 billion (see note 12f to the accounts) and constrained the cash outflow at £128 million.

Key issues

These should be the last set of accounts the Group produces on the existing basis as many of the legacy issues to which our financial performance has been vulnerable over recent years will transfer to the NDA on 1 April 2005. In addition to the items noted below, these include matters such as nuclear provisions and continuing accounting losses on Magnox electricity generation.

British Energy

As part of the arrangements with BE agreed in November 2002, BE continue to make payments for ongoing AGR fuel and spent fuel supply as if the new contracts were effective. The Secretary of State announced last year Government's commitment to contribute significantly to BE's historic nuclear fuel liabilities which we currently manage. These arrangements are going through a process of state aid approval from the European Commission and until clearance is received there has been a 'standstill' on the payments for these historic liabilities (see note 4 to the accounts).

Magnox station decommissioning costs

Last year the Group started to update decommissioning plans for the Magnox stations and recognised an additional charge of £415 million relating to cost increases in the care and preparation phases for Hinkley Point A and Bradwell. I explained in my review that as future plans were agreed it was likely that further similar charges would be incurred. Work has continued this year, which in the normal course of business would have led to a further increase in provisions. However in preparation for the establishment of the NDA the Group is working on full lifetime 'Life Cycle Baseline Plans' (LCBLs) which will form the basis for the actual discharge of liabilities from 1 April 2005 when the NDA will take responsibility for the sites. Whilst a large part of the work undertaken in preparing the existing plans will underpin the final LCBLs (which are due for completion and submission in September 2004) the work to date has raised a number of challenges to our existing strategy and assumptions. As a result, alternatives to many of the current strategies and assumptions will be explored over the coming months. Accordingly, we have taken the view that the existing provisions remain our best current estimate. We will continue to evaluate the challenges to the strategy over the course of the coming financial year (see note 4 to the accounts).

MOX plant

We continue to face a number of operational challenges with the Sellafield MOX Plant. The most recent financial forecasts for SMP, which are used both for economic appraisal and accounting for SMP contracts, has shown some deterioration from last year, reflecting recent difficulties in achieving production ramp-up and our current best estimate of the future production profile. This deterioration has caused a substantial increase in the provisions for contract losses booked this year on a standard contract accounting basis (see note 27 to the accounts). The work to date has raised a number of challenges to our existing strategy and assumptions, as a result the ongoing cash flow projections continue to support our assumption that there is no FRS 11 impairment of the asset.

Financial performance

Group turnover has increased this year by £103 million to £2,322 million. At the operating level the loss was £351 million (2003: £190 million loss before exceptionals). As explained earlier this deterioration is due to additional accounting losses on MOX production, extra Sellafield costs and continuing losses on electricity generation.

Last year's net financing charge of £134 million was dominated by 'mark to market' losses of £74 million on investments held by our Captive Insurance Subsidiaries. This year we have seen a more favourable valuation at 31 March 2004 thus the position has largely reversed, with a £61 million gain recognised this year, resulting in a substantial reduction in the Group's net financial charges.

After a contribution from joint ventures and associated undertakings of £68 million (2003: £63 million) and a small gain from the sale of fixed asset investments, the Group generated a loss before taxation of £299 million (2003: £255 million before exceptional operating costs of £833 million).

The underlying total business cash flow in 2004 has borne the full year impact of the BE standstill and containing the total cash outflow near to 2003 levels has been a major achievement.

THESE SHOULD BE THE LAST SET OF ACCOUNTS THE GROUP PRODUCES ON THE EXISTING BASIS

The table below explains how the reported cash flow reconciles to the underlying business cash flow.

	2004 £m	2003 £m
Reported cash (outflow)/inflow	(128)	109
Income/(expenditure) from the NLIP (note 1 below)	153	(254)
(Expenditure)/income from longer term deposits (note 2 below)	(159)	23
Total cash outflow from the business	(134)	(122)

The reported statutory cash flow reflects movements in cash as defined in FRS 1, 'Cash flow statements'. This does not include any income or expenditure from the NLIP, which is treated as a fixed asset investment, or longer term deposits not qualifying as cash under FRS 1.

Note 1

The income from the NLIP in 2004 represents receipts relating to interest earned during the year on the portfolio. Last year this income was offset by a withdrawal of £400 million from the NLIP, which was used to fund the discharge of nuclear liabilities. This year, whilst we have spent £510 million on the discharge of nuclear liabilities, we have funded this from other cash resources without drawing down from the NLIP.

Note 2

This year £159 million of our net expenditure has been funded by longer term deposits which have been liquidated during the year. Last year, primarily as a result of the draw down from the NLIP, there was no significant liquidation of longer term deposits.

Progress towards the NDA

Last year we reorganised the UK operations of the Group to align structurally, commercially and financially with the future NDA organisation. Whilst there continues to be some changes to this 'split' of assets and liabilities they are expected to be relatively insignificant in relation to the overall magnitude of the balance sheet. There remains work to do on the detailed accounting for the new arrangements, but we are confident that the net asset deficit will be resolved and the volatility of nuclear liabilities and legacy issues will be removed from the Group.

In this last year the strategy review and subsequent work with the DTI have further developed the model for how the Group will operate post-NDA. The analysis of the business in the segmental information in note 2 of the accounts includes some of these changes but others will only be reflected in our activities from 1 April 2004.

Accordingly the performance of the various business segments for 2003-2004 in note 2 may not be representative of the performance going forwards, for example:

Westinghouse Group: it is intended that the assets and liabilities of the Springfields site in the UK will transfer to the NDA and Westinghouse will operate the site on a manage and operate basis consistent with the agreed model for our other UK sites. As a result Westinghouse's profits before interest and taxation (absent currency considerations) are expected to slightly reduce from current levels with a commensurate reduction in risk.

British Nuclear Group currently includes a contribution from some smaller subsidiaries which form part of their potential Project Services business whose business plan is due for review and agreement with the DTI at the end of June. The current internal fee levels are the subject of ongoing negotiation with the DTI and, realistically, may finally settle to below currently assumed levels. Depending on the outcome of this further work, British Nuclear Group could generate an ongoing baseline profit before interest and taxation of between £70-£100 million.

We have previously operated a combined R&T operation which is included in the Corporate Centre in note 2 to these accounts.

From 1 April 2004 we have restructured this into a small Technology function which both provides technology direction to the businesses and manages various technology investments and a larger business, NSTS, which provides services to a range of customers (not solely other members of the Group). In the future NSTS is expected to make a small profit and the Technology function will be part of the costs of the Corporate Centre.

Spent Fuel Services: work has started to agree with the DTI the most appropriate structural and contractual arrangements for the spent fuel activity after 1 April 2005.

There has been a comprehensive review of the Corporate Centre, which has resulted in a transfer of both responsibility and costs into the businesses. From 1 April 2004 we will see this transfer between the Centre and Business Groups in the financial results and subsequently there will be reductions in the Centre costs.

We are confident that once these changes take effect and the NDA transfer is complete we will have a viable group based on a set of broadly self sufficient businesses with a small focused Corporate Centre. The Group's pre taxation profitability at circa £150 million per annum may be lower than currently experienced by the 'NewCo' business segments (contained in note 2 to the accounts) but the Group is expected to be profitable and tax paying in future years. For the first time in several years the Group should be in a position to pay annual dividends to our Shareholder beyond 2005.

Our US subsidiary BNFL Inc has two large clean-up contracts in the US. At East Tennessee Technology Park (ETTP) there is a contract to decontaminate and decommission three gaseous diffusion plant facilities and at the Idaho National Engineering and Environment Laboratory we have built the Advanced Mixed Waste Treatment Plant (AMWTP) to process and treat waste. Discussions are taking place with DoE on a government to government basis, supported by BNFL, with a view to seeking to recover part of the previously incurred losses and reduce exposure going forward. We are hopeful of a successful conclusion to these discussions although the final details will take some time to negotiate.

Treasury

The financial resources of the Group at 31 March 2004 comprise:

	2004 £m	2003 £m
Nuclear Liabilities Investment Portfolio	4,016	3,843
Investments and short-term deposits	1,522	1,822
Cash at bank and in hand	119	69
	5,657	5,734
Secretary of State's Undertaking	5,525	5,159
	11,182	10,893

At 1 April 2005 when the balance sheet is expected to be reconstructed and assets and liabilities transferred to the NDA, the NLIP and Secretary of State's Undertaking will be part of that transfer. We will be making every effort to ensure that we hand over to the NDA an NLIP worth over £4 billion. The allocation of other investments has yet to be determined.

The Group remains relatively debt free with total loans of £27 million at 31 March 2004 (2003: £51 million). The £27 million related to Westinghouse's \$50 million deliverables facility, which was fully drawn down at 31 March 2004. The main loan funding relates to the US operations of Westinghouse where there is a US\$340 million credit facility with a consortium of lending banks. At 31 March 2004 there was no cash draw down of the facility and for the major part of the year the facility has been used solely to support letters of credit.

Apart from the Captive Insurance Subsidiaries which hold equities, the investment policy for the rest of the Group is to hold funds in gilts and bank deposits, money funds and cash funds which are less vulnerable to market valuations. This keeps the Group's investment risk at a low level. From a liquidity perspective, the Group's investment policy is fairly straightforward and similarly cautious; except for the NLIP, which is mostly invested in gilts, it is largely centred around short- to medium-term

deposits, in the money market. Whilst the Captive Insurance Subsidiaries investment policy is to hold equities and fixed income investments through managed funds, the policy is designed to maintain risk within a defined limit.

Currently profits are susceptible to the rate of inflation because returns from investments to support nuclear liabilities (NLIP and the Secretary of State's Undertaking) fail to match the required revalorisation of the nuclear liabilities provision which represents Retail Price Index (RPI) plus reversal of a year's discounting (2.5%). This will remain the case until the restructuring takes place when inflation exposure will become a more usual case of matching inflationary cost increases to sales growth or increases in productivity.

The Group's policy is to hedge against specific foreign currency transactions including some substantial \$ denominated inter-group loans. The timing of the close out of these hedges is largely coincident, this year, with the financial year end which has protected reserves from an otherwise significant adjustment on the conversion of US\$ denominated assets. The closing \$:£ exchange rate as at 31 March 2004 was 1.8378 (2003: 1.5807).

Summary

Another year closer to the NDA formation and the post-NDA business model is starting to crystallise. These should be the last set of accounts the Group produces on the existing basis as next year's accounts should reflect the transfer of a substantial part of our nuclear assets and liabilities exposure to the NDA.

Whilst the Group's results continue to be overshadowed by liabilities and historic issues the underlying operational performance continues to improve with the Group now beginning to consistently set and deliver realistic targets, although the progress of the MOX plant ramp-up continues to cause us concern. We remain optimistic about the progress of the NDA formation and are looking forward to the undoubtedly testing commercial environment which it will bring.

Board of Directors

1 Hugh Collum (63)

Chairman Appointed to the Board on 21 July 1999 and became Chairman on 1 October 1999. He was formerly Executive Vice-President and Chief Financial Officer of SmithKlineBeecham plc. Until recently he was Deputy Chairman of Celltech Group plc and a Non-Executive Director of Safeway plc. He is currently a Non-Executive Director of Whitehead Mann Group plc and a member of the Advisory Board of Barclays Private Bank. He is due to retire from BNFL on 31 May 2004.

2 Mike Parker (57)

Group Chief Executive Appointed to the Board on 1 August 2003. He was formerly President and Chief Executive Officer of The Dow Chemical Company, USA. He served in a wide variety of jobs in research, manufacturing and the commercial area since he began his Dow career in 1968, working in the USA, UK, Switzerland and Hong Kong before joining the Dow Board in 1995.

3 Joe Darby (55)

Non-Executive Director Joined the Board on 23 January 2002. He was previously Chief Executive Officer and Deputy Chairman of LASMO plc. He is Non-Executive Chairman of Faroe Petroleum plc, a Non-Executive Director of John Mowlem & Company plc and a Fellow of the Institute of Petroleum.

4 Gordon Campbell (57)

Non-Executive Director Joined the Board on 1 August 2000. He is part-time Chairman of Babcock International Group PLC and former Chief Executive of Courtaulds plc. He is a Vice-President of the Royal Academy of Engineering, Non-Executive Chairman of ITI Scotland and a Non-Executive Director of Jupiter Split Trust plc. He has been appointed Non-Executive Chairman of BNFL commencing 1 June 2004.

5 David Bonser (55)

Director of BNFL ALFA and Spent Fuel Services Joined the Board on 30 September 1999. He joined BNFL in 1971 and has been a Director of Thorp, Company Development and Engineering, Waste Management and Decommissioning prior to his current position. He has been a member of the Government's Radioactive Waste Management Advisory Committee (RWMAC) and was Chairman of United Kingdom Nirex Limited until December 2001.

6 Bill Lowther (64)

Non-Executive Director Joined the Board on 1 August 2000. He was Director-General of Surface Specialties plc (UCB Films plc) until his retirement in 2002 when he was appointed as Non-Executive Chairman. Since 1998 he has been a member of the North West Business Leadership Team. He is Chairman of the Cumbria Strategic Partnership and Deputy Chairman of Securrency Pty. Ltd, a joint venture company between UCB SA and The Reserve Bank of Australia.

7 Dr Gail de Planque (59)

Non-Executive Director Joined the Board on 23 November 2000. She has served as a Commissioner with the United States Nuclear Regulatory Commission and as the Director of the Department of Energy's Environmental Measurements Laboratory in New York City. She is a Fellow and past President of the American Nuclear Society, a member of the National Academy of Engineering and the National Council on Radiation Protection and Measurements. She is President of Strategy Matters Inc., and serves as a member of the Board of Trustees of Northeast Utilities and is a Director of TXU Corp. and Landauer, Inc.

8 Brian George (68)

Non-Executive Director Joined the Board on 12 March 2001. He is a former Executive Director of Nuclear Electric plc and NNC Limited. He has worked for General Electric Company as Chief Executive of GEC Marine Limited, Vickers Shipbuilding and Engineering Limited and Yarrow Shipbuilders Limited.

9 Richard Stone (61)

Non-Executive Director Joined the Board on 1 January 2001. He retired from the Global Board of PricewaterhouseCoopers at the end of 2000. Prior to the merger with Price Waterhouse in 1998, he was Deputy Chairman of Coopers & Lybrand, and Chairman of the firm's European corporate finance activities. He is Chairman of Shearings Group Limited and Non-Executive Director of Halma plc, TR Property Investment Trust plc, Trust Union Finance (1991) plc, CSW Group Limited and Gartmore Global Trust plc.

10 Jim Currie (63)

Non-Executive Director Joined the Board on 1 November 2002. A highly experienced international civil servant, he spent many years working in Brussels and Washington. He was formerly Director General at the European Commission with responsibility for the EU's Environmental Policy and previously Director General for Customs and Indirect Taxation. He is also a Director of The Royal Bank of Scotland plc and International Adviser to Eversheds.

11 John Edwards (55)

Group Finance Director Joined the Board on 1 July 2000. He is the former Finance Director of Jaguar, Northern Electric and Meyer International plc. He is the Chairman of Magnox Electric plc and BNFL's Investment Review Panel and is a Director of Urenco Limited.

Report of the Directors

for the year ended 31 March 2004

1. The directors of British Nuclear Fuels plc present to the Shareholders their thirty-third Annual Report together with the audited accounts for the year ended 31 March 2004.

Review of the year

2. Group results

The Group loss for the year, after taxation and minority interests amounted to £194 million (2003: loss of £865 million), comprising of a loss on ordinary activities before taxation and exceptional items of £303 million (2003: loss of £261 million), exceptional income of £4 million (2003: net exceptional charge of £827 million) and a taxation credit of £105 million (2003: taxation credit £223 million). Further information on the Group's results is contained in the Financial review on pages 42 to 45.

3. Dividend

No dividend is proposed (2003: nil).

4. Activities

The main activities of the Group comprise:

- Westinghouse Group: provides fuel, services, technology, plant design and equipment to the worldwide nuclear electricity industry;
- British Nuclear Group: provides nuclear clean-up, decommissioning and environmental services together with nuclear facility management and operations to governments and the commercial nuclear industry worldwide;
- Spent Fuel Services Group: manages the customer interface between the Group and utility customers, both in the UK and overseas that send used fuel to Sellafield for recycling. It also provides a rail and sea transport service, primarily to bring spent fuel to the reprocessing plants and to return MOX fuel to customers;
- Assets, Liabilities and Financing Agency (BNFL ALFA): holds the assets and liabilities that are expected to transfer to the NDA and acts as the internal customer for the management and operations business in British Nuclear Group; and
- Corporate: mainly comprises research and technology and head office functions. The Captive Insurance Subsidiaries held by the Group are also within this area.

Information on the activities and developments of the business of the Group during the year is contained in the Chairman's statement, Chief Executive's review, Business reviews and Financial review appearing on pages 12 to 45.

5. Research and development

The Group has a significant research and development programme. During the year the Group spent a total of £98 million (2003: £109 million) on research and development, £59 million (2003: £67 million) were costs charged against profits, and £39 million (2003: £42 million) was charged to customers.

6. Personnel

The average number of people employed by the Group during the year was 23,149 (2003: 22,971). At 31 March 2004 the total number of people employed by the Group was 23,153 (2003: 23,195). Further information is given in note 5 within the Accounts on page 69.

The Group attaches importance to the involvement of its employees in the Group's development and has continued its previous practice of keeping them informed on matters affecting them as employees and on the various factors affecting the performance of the Group. Employee representatives are consulted regularly on a wide range of matters affecting the current and future interests of the employees.

The Group is committed to a policy of equal opportunities for all employees. Great care is exercised in our recruitment and selection procedures to ensure that there is no discrimination, and that training is given to meet individual needs. Applications by people with disabilities are given full and fair consideration and, wherever practical, provision is made for their special needs. The same criteria for training and promotion apply to people with disabilities as to any other employee. If employees become disabled, every effort is made to ensure their continued employment.

7. The Board of Directors

The names of the directors of the company during the year were:

Chairman and Executive Directors:

Mr H R Collum (Chairman) ♦*
Mr M D Parker (Chief Executive) — appointed 1 August 2003
Mr N Askew — resigned 31 July 2003
Mr J F Edwards
Mr D R Bonser

Non-Executive Directors:

Mr G A Campbell ♦* ♦
Mr J Darby ▲ ♦
Dr E G de Planque ▲ ♦
Mr B V George ▲* ★
Mr W Lowther ★
Mr R A Stone ★* ♦
Mr J Currie ♦ ♦

Committees:

▲ Environment, Health and Safety Committee
★ Audit Committee
♦ Remuneration Committee
+ Nominations Committee
*denote Chairman of the Committee

The Secretary of State for Trade and Industry is recorded in the company's register of directors as a Shadow Director of the company within the meaning of Section 741 of the Companies Act 1985.

References made to the Shareholder throughout this report are to the Secretary of State for Trade and Industry.

Report of the Directors

8. Directors' shareholdings and interests

No serving director held, at any time during the year, any share in, or convertible loan stock of, the company or of its subsidiaries or of any associated undertaking or joint venture, except for the Shadow Director, who holds 32,668,243 (2003: 32,668,243) ordinary £1 shares.

9. Contributions for political or charitable purposes

The Group has not made any political donations in the year (2003: £nil). Charitable contributions during the year amounted to £3.3 million (2003: £3.2 million), in support of the Group's community involvement and economic regeneration initiatives. These contributions include £1.9 million (2003: £2.2 million) to support West Cumbrian economic regeneration initiatives.

10. Policy on the payment of suppliers

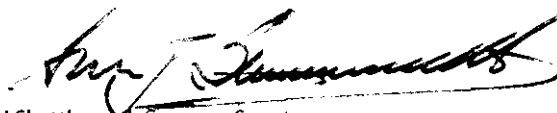
The company has continued its commitment to the Prompt Payers Code of Practice drawn up by the Confederation of British Industry (CBI), with rigorous monitoring of payment performance. The company has two main

payment terms, net monthly and 35 days. Suppliers are made aware of the terms of payment and the terms are settled when agreeing the details of each transaction. After taking account of genuine queries, 85% (2003: 80%) of invoices submitted against these terms were paid on time. The average age of invoices outstanding at 31 March 2004 was 34 days (2003: 23 days).

11. Auditors

A resolution to reappoint the auditors, Ernst & Young LLP, as the company's auditor will be proposed to the forthcoming Annual General Meeting.

By order of the Board



A J Shuttleworth Company Secretary
27 May 2004

Corporate governance

Statement of compliance

The Board is committed to achieving the highest standards of corporate governance and has committed to comply with the Combined Code issued by the United Kingdom Listing Authority (the Code).

Following the publication of the revised Combined Code by the Financial Reporting Council on 23 July 2003, a review has been undertaken within the Group with the intention to achieve compliance, where appropriate, in financial year 2004-2005.

The Board

The Board comprises a Chairman, three executive directors including a Chief Executive and seven non-executive directors. The Senior Non-Executive Director is Gordon Campbell. The non-executive directors are independent from management and are free from any business or other relationship which could materially interfere with the exercise of their independent judgement. The non-executive directors bring a wide range of experience to the Board and participate in decisions on key issues facing the Group.

Eight Board meetings are held during the year with additional meetings convened as necessary. The Board considers a number of matters specifically reserved to it, including strategic, financial and organisational issues. Appropriate and timely information is supplied to ensure all directors are properly briefed to enable the Board to discharge its duties. All directors are entitled to obtain independent professional advice at the expense of the company and have access to the advice and services of the Company Secretary.

All new Board appointments are subject to re-election by the Shareholders at the next Annual General Meeting, following their appointment. Appropriate training and briefings are available to all directors on appointment and subsequently, as necessary, taking into account existing qualifications and experience.

The Board has established five committees, the Environment, Health and Safety Committee, the Audit Committee, the Remuneration Committee, the Nominations Committee and the General Purposes Committee. Each Board committee consists solely of non-executive directors with the exception of the General Purposes Committee. All non-executive directors receive notice of each committee meeting and are entitled to attend. Only those directors who have formally been appointed to a committee have the right to vote on matters presented to it. The Company Secretary is the secretary of each committee.

Environment, Health and Safety Committee

The Environment, Health and Safety Committee seeks to provide assurance on the adequacy and implementation of the Group environment, health and safety manual, the UK environment, health and safety manual and the Group environment, health and safety inspection, audit and monitoring programme. The Committee seeks assurances on the implementation and recommendations in independent inspection/audit reports, internal reports and presentations on specific initiatives within the Group, and inspections undertaken by the regulatory bodies.

Audit Committee

The Audit Committee meets at least three times a year and reviews the effectiveness of internal control systems within the Group and the principles, policies and practices adopted in the preparation of the accounts to confirm that they comply with all statutory requirements and best practice in corporate governance. The Committee reviews both the internal audit programme, which it approves and considers the major findings arising from it and also the role and work of the external auditors.

Remuneration Committee

The Remuneration Committee makes recommendations to the Board on the remuneration of executive directors and the conditions of service to be applied. The decisions on directors' remuneration are made to and approved by the Shareholder. The Remuneration report is on pages 52 and 53.

Nominations Committee

The Nominations Committee reviews the Board structure, size and composition and makes recommendations to the Shareholder.

General Purposes Committee

The General Purposes Committee has all the powers of the Board in relation to any matters, which in the opinion of the Chairman or Chief Executive, are deemed urgent or necessary for the proper conduct of the business of the company. The Committee reports all matters undertaken by it to the next meeting of the Board.

Internal control

During the financial year, the Group continued to develop and embed the procedures necessary to implement the guidance issued by the Internal Control Working Party of the Institute of Chartered Accountants in England and Wales, published in September 1999 (the Turnbull Committee Report) and report in accordance with that guidance.

The Board acknowledges it has overall responsibility for the Group's system of internal control and for reviewing its effectiveness, whilst the role of management is to implement Board policies on risk and control. It should be noted that with regard to joint venture and associated undertakings, the level of control exercised necessarily reflects the governance framework of each entity. The Board further acknowledges that any system of internal control is designed to manage, rather than eliminate, the risk of failure to achieve business objectives. In pursuing these objectives, internal controls can only provide reasonable and not absolute assurance against material misstatement or loss.

The Board confirms that there is an ongoing process for identifying, evaluating and managing significant risk faced by the Group. This process was fully implemented across the Group for the year under review and up to the date of approval of the Annual Report and Accounts.

The process used by the Board to review the effectiveness of internal control includes the following:

- The Audit Committee reviews the effectiveness of internal control systems within the Group and refers its findings to the Board. It receives reports from the internal and external auditors as well as from business groups as appropriate;
- The Group operates a risk management process which identifies the key risks facing the business. This process is based on each business group and function identifying their key risks and the probability of those risks occurring, their impact and actions being taken to manage those risks. This information is used to produce a profile of the significant risks facing the Group. A Significant Risk Report is produced on a quarterly basis for the Group's Executive Committee;
- At the year end, before producing the statement in the Annual Report and Accounts, the Board asks each Executive to complete a Letter of Assurance confirming compliance with the Group's policies, procedures and risk management processes. The outcome of these letters is reported to the Audit and Executive Committees and thereafter to the Board. The Board, via the Audit Committee, reviews the significant risks twice a year and receives regular reports on any major issues or changes in risks; and
- The Board also receives regular reports from its Board Committees, business groups and risk management functions which include details of any control failures, together with corrective actions planned or executed, in addition to other performance reports.

Areas of non-compliance with the Combined Code

The items in the Combined Code with which the Group did not comply in full throughout the financial year were as follows:

- The Articles of Association do not currently require the executive directors to submit themselves for re-election at least every three years. However, two executive directors' service contracts provide for a notice period of one year and one for a notice period of six months, and notices can be given at any time. Non-executive directors are appointed for a fixed term not exceeding three years before being eligible for re-election; and
- The Group does not currently have any institutional investors and therefore the requirements of the Combined Code in this area are not relevant.

Going concern

During the year, the Group has continued to have a net asset deficit. At the balance sheet date the deficit was £2,895 million (2003: £2,690 million), principally as a result of the impact of the Historic Waste Management Strategy introduced in 2002, which substantially increased the level of nuclear provisions on the Group's balance sheet.

These accounts have been prepared on a going concern basis, having taken account of the Group's cash resources and relying on the Ministerial Statement made in the House of Commons on 28 November 2001 containing proposals for the management of public sector civil nuclear liabilities. Subsequent actions taken by Government have reconfirmed its commitment to address this issue which is responsible for the Group's net asset deficit position. Over the last year the draft Bill underwent pre-legislative scrutiny of the House of Commons Trade and Industry Select Committee and now comprises part-one of the Energy Bill which is making its way through the legislative process. The Bill, which will result in a significant improvement in the Group's financial position, is expected to be enacted this summer.

Remuneration report

In line with best practice the Board will be submitting this report on directors' remuneration for the financial year ended 31 March 2004 to the Shareholder at the forthcoming Annual General Meeting.

Remuneration Committee

The following directors, all of whom are independent non-executive directors, were members of the Remuneration Committee during the year ended 31 March 2004:

Gordon Campbell (Chairman)
Jim Currie
Joe Darby
Gail de Planque

The members of the Remuneration Committee have no financial interest in the matters to be decided, no potential conflicts of interest arising from cross-directorships and no day-to-day involvement in running the business.

The Remuneration Committee during the period received advice from Towers Perrin and Mercer Human Resource Consulting Limited (who were appointed by the company on behalf of the Remuneration Committee).

The Remuneration Committee generally meets three times a year, making recommendations to the Shareholder on the terms and conditions, including annual remuneration and bonus awards, for the executive directors. The Chairman and the Chief Executive normally attend these meetings, except when their own salaries are discussed.

Policy on remuneration of executive directors

The remuneration policy for executive directors is to offer a competitive remuneration package which will attract and retain the highest calibre of executive and to ensure that individual rewards and incentives are directly aligned with individual business performance, the performance of the Group and the interests of the Shareholder. In order to ensure this approach is competitive, a group of UK and international companies has been selected, and our remuneration components are carefully compared against this group. The company's policy is to be similar to median levels of this group.

The remuneration arrangements, which meet the provisions of Schedule A to the Combined Code, include basic salary and benefits, performance related bonus and pensions. The main elements are:

i. Basic salary and benefits

The level of basic salary and benefits is determined by the Remuneration Committee and approved by the Shareholder, taking into account the performance of the individual and advice and information from independent sources on the rates of salary and benefits for similar positions in a comparator group of companies. Individual salaries of executive directors are reviewed annually by the Remuneration Committee. Benefits normally include the provision of a car, fuel and private healthcare.

ii. Performance related bonus

The performance related bonus targets are agreed at the beginning of each year by the Remuneration Committee and approved by the Shareholder. Annual performance bonuses, which this year have a maximum payment of 30% of basic salary, are earned for the achievement of targets linked to the Group's performance in safety, profit before taxation and cash flows. The Shareholder approves the amount of bonus payable to each executive director after considering the achievements against targets and after recommendation from the Remuneration Committee.

iii. Pensions

David Bonser is an active member of the Combined Pension Scheme of the UKAEA which pays an annual pension of one-eightieth plus three-eightieths lump sum of final pensionable pay for each year of service. No employer contributions have been made to this scheme during the year. Details of the pension benefits for David Bonser are as follows:

Table A. Pension benefits

	2004 £	2003 £	Increase £	Increase excluding inflation/ contributions* £
Accrued pension benefits	92,051	85,915	6,136	3,730
Accumulated lump sum	276,153	257,746	18,407	11,190
Transfer value*	1,574,683	1,451,801	122,583	112,532*

*The transfer value represents a potential liability of the pension scheme and is not a sum paid or payable to David Bonser. The increase in transfer value of £112,532 is net of contributions made by David Bonser himself.

Pension contributions of £11,340 (2003: £34,020) for Norman Askeew and £28,750 (2003: £27,398) for John Edwards were made to their personal defined contribution pension schemes. Mike Parker receives a monthly allowance of 10% of his salary, through his salary and makes his own pension arrangements.

Service agreements

The company's policy in relation to the duration of contracts with directors is that executive directors' contracts generally continue until termination by either party, subject to the required notice, or until retirement date. The notice period under the service contracts of executive directors will not normally exceed 12 months. There are no predetermined special provisions for executive and non-executive directors with regard to compensation for loss of office. Cases of early termination are considered by the Remuneration Committee and the Shareholder, who determine the level of compensation payments.

Information regarding executive directors' service contracts is summarised in the table below:

	Date of current contract	Notice period from company	Notice period from director
Mike Parker	1 August 2003	12 months	6 months
John Edwards	1 July 2000	12 months	3 months
David Bonser	30 September 1999	6 months	3 months

The normal retirement age for each of the executive directors is 60, with the exception of Mike Parker, who has a normal retirement age of 62.

Chairman and non-executive directors

The original date of appointment as a director of the company and the scheduled date of termination of the current appointment periods are as follows:

	Date first appointed	Date of termination
Hugh Collum	21 July 1999	31 May 2004
Gordon Campbell	1 August 2000	31 March 2007*
Jim Currie	1 November 2002	31 March 2005
Joe Darby	23 January 2002	31 March 2005
Brian George	12 March 2001	30 June 2004
Bill Lowther	1 August 2000	30 June 2006
Gail de Planque	23 November 2000	30 June 2004
Richard Stone	1 January 2001	30 June 2004

*Subject to re-election at the 2004 Annual General Meeting.

Remuneration report

None of the non-executive directors have service agreements. With the exception of Hugh Collum, each non-executive director's Letter of Appointment provides for an initial period of three years. Letters of Appointment do not provide for a notice period. Non-executive directors do not normally serve longer than two consecutive periods of three years; such reappointment is subject to the approval of the Shareholder.

Hugh Collum is due to retire on 31 May 2004. The Board of Directors has appointed Gordon Campbell as Non-Executive Chairman commencing 1 June 2004. Gordon Campbell's Letter of Appointment, as Non-Executive Chairman, provides for a period of three years ending 31 March 2007 and is terminable by the company at six months' notice.

The company's Articles of Association do not require the executive and non-executive directors to retire by rotation.

Directors' remuneration

Table B below summarises total directors' remuneration. Benefits include non-cash benefits comprising the provision of a company car and private healthcare.

The remuneration of the non-executive directors takes the form of fees, which are approved by the Shareholder. On 1 July 2003 the fee for each non-executive director increased from £20,000 to £25,000 per annum. In addition, each non-executive director receives an additional £5,000 per annum if they serve as a Chairman of a Board Committee or £2,500 per annum if appointed a Member of a Committee, except the General Purposes Committee, for which no fees are paid. The non-executive directors are reimbursed reasonable travel expenses.

Fees paid to former directors

During the year the former directors as detailed in Table C below received payments from the Group. These payments relate to the provision of consultancy services within areas of their individual expertise.

Table C. Fees paid to former directors

	2004 £	2003 £
Greg Butler	78,109	65,534
Neville Chamberlain	—	6,226
John Rimington	3,875	5,025
Bill Wilkinson	38,708	38,255

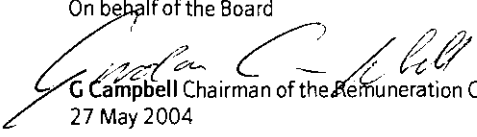
Table B. Directors' remuneration

	Basic salary and fees		Annual bonus		Benefits		Total	
	2004 £	2003 £	2004 £	2003 £	2004 £	2003 £	2004 £	2003 £
Chairman								
Hugh Collum	165,000	157,500	—	—	26,098	24,178	191,098	181,678
Executive								
Norman Askew	125,317	375,950	—	121,432	6,321	7,082	131,638	504,464
Mike Parker	300,000	—	58,570	—	87,153*	—	445,723	—
David Bonser	207,000	198,790	40,303	67,986	17,429	16,671	264,732	283,447
John Edwards	287,500	273,980	55,976	88,222	17,872	17,345	361,348	379,547
Chris Loughlin	—	32,167	—	—	—	2,764	—	34,931
Non-Executive								
Gordon Campbell	31,250	27,500	—	—	—	—	31,250	27,500
Jim Currie	28,750	10,416	—	—	—	—	28,750	10,416
Joe Darby	28,750	25,000	—	—	—	—	28,750	25,000
Brian George	31,250	27,500	—	—	—	—	31,250	27,500
Bill Lowther	26,250	22,500	—	—	—	—	26,250	22,500
Gail de Planque	28,750	25,000	—	—	—	—	28,750	25,000
Richard Stone	31,250	27,500	—	—	—	—	31,250	27,500
							1,600,789	1,549,483
Fees paid to Gail de Planque as a Non-Executive Director of BNFL Inc., a wholly owned subsidiary of the company							18,081	22,792
Compensation and pension payments to former director							—	1,041,031
							1,618,870	2,613,306

*Benefits paid to Mike Parker relate primarily to relocation and accommodation costs.

Emoluments for Norman Askew and Mike Parker represent payments for the part of the year during which they held office, as indicated in note 7 of the Report of the Directors.

On behalf of the Board


G Campbell Chairman of the Remuneration Committee
27 May 2004

Statement of Directors' responsibilities

in respect of the preparation of the accounts

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

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

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

The directors confirm that the accounts comply with the above requirements.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy, at any time, the financial position of the Group and to enable them to ensure that the accounts comply with the Companies Act 1985. They have a general responsibility for taking such steps as are reasonably open to them for safeguarding the assets of the Group, and to prevent and detect fraud and other irregularities.

Independent Auditors' report

to the members of British Nuclear Fuels plc

We have audited the Group's accounts for the year ended 31 March 2004 which comprise the Consolidated Profit and Loss Account, Consolidated Balance Sheet, Company Balance Sheet, Consolidated Cash Flow Statement and the notes there to, Consolidated Statement of Total Recognised Gains and Losses and the related notes 1 to 35. These accounts have been prepared on the basis of the accounting policies set out therein.

This report is made solely to the company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an Auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and Auditors

As described in the Statement of Directors' responsibilities the company's directors are responsible for the preparation of the accounts in accordance with applicable United Kingdom law and accounting standards.

Our responsibility is to audit the accounts in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards.

We report to you our opinion as to whether the accounts give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the accounts, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions with the company is not disclosed.

We read other information contained in the Annual Report and consider whether it is consistent with the audited accounts. This other information comprises the Chairman's statement, Chief Executive's review, Business review, Financial review, Report of the Directors, Corporate Governance statement, Remuneration report and financial statistics. We consider the

implications for our report if we become aware of any apparent misstatements or material inconsistencies with the accounts. Our responsibilities do not extend to any other information.

Basis of audit opinion

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

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

Fundamental uncertainty

In forming our opinion on the full annual accounts, we have taken note of the fundamental uncertainty inherent in the estimation of nuclear liabilities which is described in note 24a. Our opinion is not qualified in this respect.

Opinion

In our opinion the accounts give a true and fair view of the state of affairs of the company and of the Group as at 31 March 2004 and of the loss of the Group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.



Ernst & Young LLP Registered Auditor
Manchester
27 May 2004

Consolidated profit and loss account

for the year ended 31 March

	Note	2004			2003		
		Operations before exceptional items £m	Exceptional items (note 4) £m	Total £m	Operations before exceptional items £m	Exceptional items (note 4) £m	Total £m
Turnover		2,504	—	2,504	2,412	—	2,412
Less: share attributable to joint ventures		(182)	—	(182)	(193)	—	(193)
Group turnover		2,322	—	2,322	2,219	—	2,219
Operating costs and expenses	3	(2,673)	—	(2,673)	(2,409)	(833)	(3,242)
Group operating loss		(351)	—	(351)	(190)	(833)	(1,023)
Operating profit — joint ventures		25	—	25	26	—	26
— associated undertakings		43	—	43	37	—	37
Profit on sale of fixed assets	6	—	4	4	—	6	6
(Loss)/profit before investment income, interest and taxation		(283)	4	(279)	(127)	(827)	(954)
Investment income	7	652	—	652	683	—	683
Interest payable and similar charges	8	(672)	—	(672)	(817)	—	(817)
(Loss)/profit on ordinary activities before taxation		(303)	4	(299)	(261)	(827)	(1,088)
Taxation on (loss)/profit on ordinary activities	9	105	—	105	152	71	223
(Loss)/profit on ordinary activities after taxation		(198)	4	(194)	(109)	(756)	(865)
Profit attributable to minority interests		—	—	—	—	—	—
(Loss)/profit transferred to reserves		(198)	4	(194)	(109)	(756)	(865)

Consolidated statement of total recognised gains and losses

for the year ended 31 March

	2004 £m	2003 £m
Loss for the financial year	(194)	(865)
Currency translation differences	(10)	18
Total gains and losses recognised since the last Annual Report and Accounts	(204)	(847)

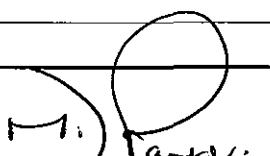
Consolidated balance sheet

as at 31 March

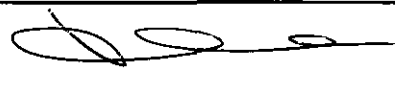
	Note	2004		2003	
		£m	£m	£m	£m
Fixed assets					
Intangible assets	10		634		768
Tangible assets	11		7,174		7,487
Investments:	12				
Joint ventures:					
Share of gross assets		708		702	
Share of gross liabilities		(675)		(669)	
		33		33	
Associated undertakings		109		99	
Nuclear Liabilities Investment Portfolio		4,016		3,843	
Other		3		3	
			4,161		3,978
			11,969		12,233
Current assets					
Stocks	13	517		464	
Debtors:					
Amounts falling due within one year	14	946		812	
Amounts falling due after more than one year:					
Customer recoverable relating to nuclear liabilities	15	4,631		4,735	
Secretary of State's Undertaking	16	5,525		5,159	
Other debtors		132		241	
Total amounts falling due after more than one year		10,288		10,135	
Investments and short-term deposits	17	1,522		1,822	
Cash at bank and in hand		128		72	
		13,401		13,305	
Creditors: amounts falling due within one year	18	(1,426)		(2,193)	
Net current assets			11,975		11,112
Total assets less current liabilities			23,944		23,345
Creditors: amounts falling due after more than one year	19	(4,895)		(4,000)	
Provisions for liabilities and charges	23	(21,944)		(22,035)	
			(26,839)		(26,035)
Net liabilities			(2,895)		(2,690)
Capital and reserves					
Called up share capital	28	33		33	
Profit and loss account	29	(2,931)		(2,727)	
Shareholders' funds	30		(2,898)		(2,694)
Minority interests			3		4
			(2,895)		(2,690)



Hugh R Collum Chairman
27 May 2004



Mike Parker Chief Executive
27 May 2004

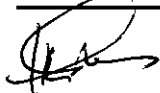


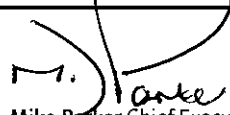
John Edwards Group Finance Director
27 May 2004

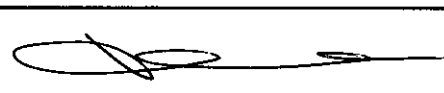
Company balance sheet

as at 31 March

	Note	2004		2003	
		£m	£m	£m	£m
Fixed assets					
Tangible assets	11	8,158		8,306	
Investments	12	5,175		5,009	
		13,333		13,315	
Current assets					
Stocks	13	80		82	
Debtors:					
Amounts falling due within one year	14	2,612		2,704	
Amounts falling due after more than one year:					
Customer recoverable relating to nuclear liabilities	15	9,789		9,022	
Other debtors		127		235	
Total amounts falling due after more than one year		9,916		9,257	
Investments and short-term deposits	17	821		1,146	
Cash at bank and in hand		36		3	
		13,465		13,192	
Creditors: amounts falling due within one year	18	(2,906)		(4,373)	
Net current assets			10,559		8,819
Total assets less current liabilities			23,892		22,134
Creditors: amounts falling due after more than one year	19	(6,248)		(5,382)	
Provisions for liabilities and charges	23	(17,411)		(16,444)	
			(23,659)		(21,826)
Net assets			233		308
Capital and reserves					
Called up share capital	28		33		33
Profit and loss account	29		200		275
Shareholders' funds	30		233		308


Hugh R Collum Chairman
 27 May 2004


Mike Parker Chief Executive
 27 May 2004


John Edwards Group Finance Director
 27 May 2004

Consolidated cash flow statement

for the year ended 31 March

	Note	2004 £m	2003 £m
Net cash (outflow)/inflow from operating activities	i	(169)	15
Dividends from joint ventures and associated undertakings	ii	28	43
Returns on investment and servicing of finance	iii	263	306
Taxation	iv	32	10
Capital expenditure and financial investment	v	(460)	(209)
Acquisitions and disposals	vi	35	41
Net cash (outflow)/inflow before use of liquid resources and financing		(271)	206
Management of liquid resources	vii	159	(23)
Financing	viii	(16)	(74)
(Decrease)/increase in cash in the year		(128)	109

Notes to the consolidated cash flow statement

for the year ended 31 March

Reconciliation of net cash flow to net movement in net funds

	2004 £m	2003 £m
(Decrease)/increase in cash in the year	(128)	109
Repayment of loans and finance leases	16	74
(Withdrawal from)/transfers to investments and deposits not qualifying as cash	(159)	23
Change in net funds resulting from cash flows	(271)	206
Unrealised losses on investments held by Captive Insurance Subsidiaries	—	(74)
Reversal of previously recognised losses on investments held by Captive Insurance Subsidiaries	61	—
Exchange adjustments	(15)	2
Movement in net funds in the period	(225)	134
Opening net funds	1,837	1,703
Closing net funds	1,612	1,837

Analysis of changes in net funds

	At 1 April 2003 £m	Cash flow £m	Non-cash movements £m	At 31 March 2004 £m
Cash at bank and in hand	72	61	(5)	128
Cash in short-term deposits	316	(183)	(10)	123
Overdrafts (note 18)	(3)	(6)	—	(9)
Loans due within one year (note 18)	385	(128)	(15)	242
Loans due after one year (note 19)	(30)	(2)	5	(27)
Finance leases (note 18)	(21)	17	4	—
Current asset investments	(3)	1	—	(2)
	1,506	(159)	52	1,399
	1,837	(271)	46	1,612

Non-cash movements relate primarily to the reversal of previously recognised losses on investments held by Captive Insurance Subsidiaries. Other non-cash movements relate to exchange losses on retranslation of current asset investments denominated in foreign currency.

Notes to the consolidated cash flow statement continued

	2004 £m	2003 £m
Operating loss	(351)	(1,023)
Depreciation/amortisation/impairment charges	553	774
Nuclear provisions charge	85	436
Nuclear provisions release/expenditure	(604)	(524)
Other provisions charge	252	344
Other provisions release/expenditure	(250)	(318)
Decrease in debtors	7	198
Increase in creditors	109	71
Increase in stock and work in progress	(62)	(94)
Increase in advance payments	94	156
Grants released	(2)	(1)
Investment provisions release	—	(4)
i. Net cash (outflow)/inflow from operating activities	(169)	15
Dividends from joint ventures and associated undertakings		
Dividends from joint ventures	20	35
Dividends from associated undertakings	8	8
ii. Dividends from joint ventures and associated undertakings	28	43
Returns on investment and servicing of finance		
Interest received	296	309
Interest paid	(29)	(18)
Income from other investments	—	17
Dividends paid to minority interests	(1)	—
Bank charges	(3)	(2)
iii. Returns on investment and servicing of finance	263	306
Taxation		
UK corporation taxation received	35	17
Overseas taxation paid	(3)	(7)
iv. Taxation	32	10
Capital expenditure and financial investment		
Purchase of tangible fixed assets	(311)	(471)
Proceeds from disposal of tangible fixed assets	4	8
Cash (invested in)/received from Nuclear Liabilities Investment Portfolio	(153)	254
v. Capital expenditure and financial investment	(460)	(209)
Acquisitions and disposals		
Acquisitions of subsidiary undertakings	—	(1)
Net cash acquired with subsidiary undertakings	—	3
Disposal of associated undertakings (note 12d)	35	—
Loans repaid by associated undertakings	—	39
vi. Acquisitions and disposals	35	41
Management of liquid resources		
Withdrawal from/(transfers to) investments and deposits not qualifying as cash	159	(23)
vii. Management of liquid resources	159	(23)
Financing		
Repayment of loans	(15)	(73)
Finance lease repayments	(1)	(1)
viii. Financing	(16)	(74)

Notes to the accounts

1. Accounting policies

a. Accounting convention

These accounts have been prepared on a going concern basis, having taken account of the Group's cash resources and relying on the Ministerial Statement made in the House of Commons on 28 November 2001 containing proposals for the management of public sector civil nuclear liabilities. Subsequent actions taken by Government have reconfirmed its commitment to address this issue which is responsible for the Group's net asset deficit position. Over the last year the draft Bill underwent pre-legislative scrutiny of the House of Commons Trade and Industry Select Committee and now comprises part one of the Energy Bill which is making its way through the legislative process. The Bill, which will result in a significant improvement in the Group's financial position, is expected to be enacted this summer.

The accounts have been prepared under the historical cost convention, modified to include the market value of certain current asset investments, and in accordance with all applicable United Kingdom accounting standards. FRS 17 Retirement Benefits has continued to be implemented in the year in accordance with the transitional arrangements in the standard. This will in future years, on the timescales set out in the standard, cause a change in the accounting policy; additional disclosure can be found within note 11 of the accounting policies and note 32 of the Notes to the accounts.

b. Basis of consolidation

The consolidated accounts include the accounts of British Nuclear Fuels plc and all its subsidiary undertakings.

Entities in which the Group holds an interest on a long-term basis and which are jointly controlled by the Group and one or more other venturers under a contractual arrangement, are treated as joint ventures. In the consolidated accounts, joint ventures are accounted for using the gross equity method. Entities, other than subsidiaries or joint ventures, in which the Group has a participating interest and over whose operating and financial policies the Group exercises a significant influence are treated as associated undertakings. In the consolidated accounts, associated undertakings are accounted for using the equity method.

c. Goodwill and other intangible assets

Goodwill arising on consolidation (note 10), representing the excess of purchase consideration over the fair value of identifiable assets and liabilities acquired, is capitalised and amortised on a straight-line basis over its useful economic life up to a maximum of 20 years (acquisitions from 1 April 1998) or written off against reserves in the year of acquisition (acquisitions before 1 April 1998). Capitalised goodwill is reviewed for impairment at the end of the first full financial year following the acquisition and in other periods if events or changes in circumstances indicate that the carrying value may not be recoverable. If a subsidiary, associated undertaking or joint venture is subsequently sold or closed, any goodwill arising on acquisition that was written off directly to reserves or that has not been amortised through the profit and loss account is taken into account in determining the profit or loss on sale or closure.

For acquisitions of associated undertakings and joint ventures before 1 April 1998, the consolidated accounts include the Group's share of net assets. For acquisitions after 1 April 1998, the consolidated accounts include the Group's share of net assets together with the balance of unamortised goodwill. Unless otherwise stated, the acquisition method of accounting has been adopted. Under this method, the results of subsidiary and associated undertakings and joint ventures acquired or disposed of in the year are included in the consolidated profit and loss account from the date of acquisition or up to the date of disposal.

Intangible assets, other than goodwill (note 10), are capitalised at cost and amortised on a straight-line basis over their estimated useful lives but no longer than 20 years. The carrying value of intangible assets is reviewed for impairment at the end of the first full financial year following acquisition and in other periods if events or changes in circumstances indicate that the carrying value may not be recoverable. Licences are capitalised and amortised on a straight-line basis over their useful economic life of 12 years.

d. Turnover

Turnover, which is stated net of value added taxation, represents the invoiced value of products delivered and services rendered to outside customers. For contracts entered into for the provision of services extending over a period of years (long-term contracts), turnover represents the sales value of work done in the year including, where appropriate, estimates of amounts not yet invoiced. For electricity generation, turnover represents amounts receivable for sales of electricity through a combination of bilateral contracts, exchange deals and the balancing mechanism of the electricity trading arrangements effective from 27 March 2001.

Substantial payments in advance are held as part of the contractual arrangements under which nuclear fuel services are provided to a number of customers. Interest income earned on these contractual advance payments is recognised as part of turnover on the contracts concerned (note 7). As the anticipated financing income on these contractual advance payments formed an integral part of the negotiation of the commercial terms, this presentation more fairly reflects the commercial terms.

e. Long-term contracts

Profits on long-term contracts are taken in the year in which the services are provided, in a manner appropriate to the stage of completion of the contracts and the nature of the business concerned. Profits are determined proportionate to the prudently assessed overall forecast profitability of the contracts after allowing for contingencies. Full provision is made for losses on contracts in the year in which they are first identified (note 27).

f. Nuclear liabilities

The accounts include provisions for the Group's obligations in respect of nuclear liabilities, being liabilities in respect of the costs associated with nuclear decommissioning, waste management, and reprocessing of fuel from the Group's reactors (note 24). These provisions are based on the latest technical assessments of the processes and methods likely to be used in the future and represent best estimates. They are derived from a

1. Accounting policies continued

f. Nuclear liabilities continued

combination of the latest technical knowledge available, the existing regulatory regime, commercial agreements and using statistical modelling techniques to evaluate the impact of a range of possible alternative outcomes. The Group's obligations are reviewed on a continual basis and estimates and hence provisions are updated accordingly. Where some or all of the expenditure required to settle a provision is expected to be recovered from another party, in accordance with FRS 12, the recoverable amount is treated as an asset. In respect of waste management or reprocessing the recoverable amounts are included in debtors (note 15), whereas amounts which relate to decommissioning are included in fixed assets (note 11a) and debtors where plants are not yet commissioned. In the profit and loss account, the provisions charges are net of recoveries from customers.

Nuclear provisions are stated in the balance sheet at current price levels discounted at an appropriate real rate of return to take account of the timing of payments. Each year the financing charges in the profit and loss account include a revalorisation charge which reflects the need to remove one year's discount from provisions made in prior years and the restatement of these provisions to current price levels.

In respect of the Historic Waste Management Strategy referred to in the 'Background to Nuclear Liabilities' on pages 95 to 97 and in note 24, the accounting treatment varies from the normal Group procedures. Despite the extensive work undertaken, the nature of wastes, the length of time for which they have been stored and the age of the storage facilities mean that much further work will be required over a number of years to confirm and further refine this strategy. The Board has recorded its best estimate of the related liabilities based on available knowledge, including a normal level of cost contingency. This estimate would normally be required to include risk, which means the financial implications of a range of possible alternative outcomes associated with the treatment of these wastes. In this case however, the level of uncertainty associated with these alternatives is such that the Board has been unable to quantify the financial impact of the range of alternative outcomes with reasonable certainty.

The Group's obligations for nuclear liabilities fall into the following categories:

- **Decommissioning**

Provisions are made for the costs (discounted) of decommissioning the Group's radioactive facilities and thereby reducing the radiological hazard. These decommissioning activities address the demolition of facilities and the management of the associated waste. The extent of decommissioning during the next century will be defined by considering both the requirements to reduce radioactive discharges and to protect the workforce by restricting dose uptake. From a safety or environmental viewpoint complete removal of all facilities on all sites may not be justified. The provisions take account of such issues and consider both facilities which are already operating and those which are expected to be commissioned as part of fulfilling the Group's waste management obligations.

For facilities that have been commissioned, provisions are recognised in full and the discounted costs are capitalised as part of the costs of the asset and depreciated accordingly (note 11). To the extent that costs are recoverable from third parties, they are treated as residual values of the assets concerned and depreciation is adjusted accordingly. Changes in estimates are treated as adjustments to the assets concerned.

Radioactive waste materials arising as a result of the Group's operations give rise to liabilities reflecting the cost of treating and disposing of them. In some instances the provisions so created cover the cost of constructing and decommissioning of plants to manage those wastes. As a result, long before those waste management plants are built and commissioned, the costs of doing so have been provided in accordance with the waste management accounting policy below. Once built, the waste management plants are treated as fixed assets, the costs of which are capitalised and depreciated over the life of the plant. This depreciation charge utilises the provisions already established. On commissioning, the decommissioning costs are capitalised and depreciated accordingly.

- **Waste management**

The costs associated with waste products, for which an authorised disposal route is already in use, principally low-level waste at present, are written off in the year in which they occur. Provisions are made for the treatment, handling and disposal of the Group's remaining waste products. The provisions are based on discounted forecast cash flows, which include both capital and operating expenditure, and are recognised as waste management obligations arise.

- **Reprocessing of fuel**

Provision is made for the defuelling, reprocessing and waste management of the spent nuclear fuel from the Group's reactors in proportion to the amount of fuel burnt. Due to the nature of the nuclear fuel process there will be some unburnt fuel in the reactors at station closure. The provisions relating to this fuel are charged to the profit and loss account over the estimated useful life of each reactor on a straight-line basis.

g. Research and development expenditure

Research and development expenditure on projects not specifically recoverable directly from customers is charged to the profit and loss account in the year in which it is incurred (note 3). Expenditure on products for which firm orders have been received is held as part of the value of stocks and work in progress for recovery against the sales value of the initial orders.

h. Tangible fixed assets

Tangible fixed assets (other than assets in the course of construction) are stated in the balance sheet at cost (including decommissioning costs where appropriate see accounting policy 1f) less accumulated depreciation. Assets in the course of construction are stated at cost and are not depreciated until commissioned. The carrying values of tangible fixed assets are reviewed for impairment if events or changes in circumstances indicate that a provision for impairment is required, or if estimated remaining useful economic lives exceed 50 years. Accumulated depreciation includes any additional charges made where necessary to reflect impairments in value.

Notes to the accounts continued

1. Accounting policies continued

h. Tangible fixed assets continued

Depreciation is calculated to write off the historical cost less residual value of assets, generally by equal annual instalments unless a throughput basis is considered more appropriate, over the period assessed as their useful lives. The periods used for depreciation purposes are:

- Buildings 10 to 60 years;
- Plant and machinery 10 to 20 years; and
- Fixtures, fittings, tools and equipment 3 to 10 years.

Provision is not made for depreciation on freehold land or assets in the course of construction. Leasehold land is amortised over the period of the lease. To the extent that costs are recoverable from third parties, they are treated as residual values of the assets concerned and depreciation is adjusted accordingly.

The Group has commercial arrangements in place for Thorp, which recover capital costs of that plant under reprocessing contracts over a shorter period than the plant's potential economic life. In order to maintain a proper matching for accounting purposes of contract income and related costs, an accrual is made for future depreciation recovered over the contract period, which will be released over the remaining useful economic life of the plant once the related reprocessing contracts are complete. This is referred to as the 'Depreciation matching accrual' in notes 18 and 19.

Capital grants are treated as deferred income and transfers are made to the profit and loss account, generally by equal annual instalments, over the period used for depreciation purposes for the assets to which they relate (notes 3, 18 and 19).

i. Fixed asset investments

Fixed asset investments comprise investments in and loans to subsidiary and associated undertakings and joint ventures, together with investment portfolios held to fund certain long-term nuclear liabilities (note 12f).

The Nuclear Liabilities Investment Portfolio is maintained as a long-term fund which is earmarked to meet long-term nuclear liabilities as they fall due. Given the nature and purpose of this fund, it is classified in fixed asset investments. The fund comprises a portfolio of Government gilt-edged securities (gilts) and other investments and a managed portfolio of gilts and other investments.

The gilts intended to be held to redemption are stated in the balance sheet on the basis of cost adjusted for the amortisation of any premium or discount arising at purchase. The premium or discount is amortised over the life of the gilts as a constant percentage of the carrying value in order to bring the gilts to face value by the redemption date. If sold before redemption the difference between proceeds and the amortised value is taken to the profit and loss account in the year of realisation. The managed portfolio is stated in the balance sheet at cost.

The carrying values of investments are reviewed for impairment if events or changes in circumstances indicate that a provision for impairment is required.

j. Current asset investments and short-term deposits

Current asset investments and short-term deposits comprise short and medium-term gilt investments intended to be held to redemption, short and medium-term managed investments and other short-term investments (note 17). Current asset investments are stated at the lower of cost and estimated net realisable value.

k. Stocks and work in progress

Stocks and work in progress (note 13) are valued at cost or net realisable value, whichever is the lower, and in the case of work in progress, after deduction of progress payments. Cost where appropriate includes a proportion of all production overhead expenses.

l. Pensions and post-retirement benefits

The Group provides pension schemes for the benefit of the majority of its employees (note 32). The schemes are funded by contributions, partly from the employees and partly from the Group, to separately administered funds.

For the Combined Pension Scheme, contributions are paid to and benefits are paid by HM Government via the Consolidated Fund. In respect of the Electricity Supply Scheme and the Group Pension Scheme the company operates defined benefit pension schemes which require contributions to be made to separately administered funds. Westinghouse Electric Company and its subsidiaries provide post-retirement benefits in the form of pensions, defined medical, dental and life insurance benefits for eligible retirees and dependants.

The contributions to each of these funds are based on independent actuarial valuations designed to secure the benefits as set out in the rules. Contributions are charged in the profit and loss account so as to spread the cost of pensions over the employees' working lives with the company. The regular cost is attributed to individual years using recognised actuarial methods. Variations in pension costs, which are identified as a result of actuarial valuations, are amortised over the average expected remaining working lives of employees in proportion to their expected payroll costs.

The disclosures as required by FRS 17 Retirement Benefits are detailed in note 32.

m. Deferred taxation

Deferred taxation is recognised in respect of all timing differences that have originated, but not reversed at the balance sheet date, with the following exceptions:

- Deferred taxation assets are only recognised if it is considered more likely than not that there will be suitable profits from which the future reversal of the underlying timing differences can be deducted;
- Provision is made for gains on disposal of fixed assets that have been rolled over into replacement assets only where, at the balance sheet date, there is a commitment to dispose of the replacement assets; and
- Provision is made for the taxation that would arise on remittance of the retained earnings of overseas subsidiaries only to the extent that, at the balance sheet date, dividends have been accrued as receivable.

1. Accounting policies continued

m. Deferred taxation continued

Deferred taxation is measured on a non-discounted basis at the taxation rates that are expected to apply in the periods in which timing differences reverse, based on taxation rates and laws enacted or substantively enacted at the balance sheet date (note 26).

n. Foreign currencies

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction or at the contracted rate if the transaction is covered by a forward exchange contract. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance sheet date or, if appropriate, at the forward contract rate. All exchange differences are taken to the profit and loss account.

The accounts of overseas subsidiary and associated undertakings and joint ventures are translated at the rate of exchange ruling at the balance sheet date. The exchange difference arising on the retranslation of opening net assets is taken to reserves (note 29).

o. Derivatives and commodity contracts

The Group uses forward foreign currency contracts and currency options to reduce foreign exchange rate exposure on certain assets, liabilities and firm commitments. These are accounted for as hedges, with gains and losses being recognised when the hedged transaction takes place.

The Group enters into contracts to sell electricity generated by its power stations. The principal contracts for physical delivery are accounted for either on the spot or forward price, depending on the nature of the contract.

These forward contracts are accounted for as hedges, with gains and losses recognised when the hedged transaction takes place.

Loss making contracts are provided for.

p. Captive Insurance Subsidiaries

Investments are stated at the lower of cost and market value at the balance sheet date and are included in current asset investments. The gains or losses on the change in market values and on disposal of investments are taken to the profit and loss account. Gains in market values are only recognised to the extent that they represent reversals of previous impairment losses. Where there is a disposal of part of an investment holding, the gain or loss arising is calculated by reference to the average unit value of the total holding. Full provision is made for all claims incurred, but not settled at the balance sheet date, on the basis of the most up-to-date information (note 27).

q. Leases

Assets held under finance leases are capitalised in the balance sheet and are depreciated over their useful lives. The interest element of the rental obligations is charged to the profit and loss account over the period of the lease and represents a constant proportion of the balance of capital repayments outstanding.

Rentals under operating leases are charged on a straight-line basis over the lease term, even if the payments are not made on such a basis.

r. Liquid resources

Liquid resources comprise current asset investments and short-term deposits excluding deposits repayable on demand.

Notes to the accounts continued

2. Segmental information

a. Business segment analysis

	Westinghouse £m	British Nuclear Group £m	Spent Fuel Services £m	Corporate £m	Subtotal £m	BNFL ALFA £m	Total £m
2004							
Total sales	1,125	1,721	107	172	3,125	1,449	4,574
Inter-segment sales	(79)	(1,623)	(50)	(150)	(1,902)	(350)	(2,252)
Sales to third parties	1,046	98	57	22	1,223	1,099	2,322
Operating profit/(loss) before amortisation	95	161	18	(31)	243	(551)	(308)
Amortisation charges	(41)	—	—	(2)	(43)	—	(43)
Operating profit/(loss)	54	161	18	(33)	200	(551)	(351)
Share of operating profit – joint ventures	—	25	—	—	25	—	25
— associated undertakings	—	—	—	43	43	—	43
(Loss)/profit on sale of fixed assets (note 6)	(2)	—	—	—	(2)	6	4
Profit/(loss) before interest, taxation and exceptional items	54	186	18	10	268	(551)	(283)
Exceptional items (note 4)	(2)	—	—	—	(2)	6	4
Profit/(loss) before interest and taxation	52	186	18	10	266	(545)	(279)
Inter-segment interest (payable)/receivable	(25)	—	—	25	—	—	—
Other (interest payable)/investment income	(10)	5	1	102	98	(118)	(20)
Profit/(loss) before taxation and exceptionals	19	191	19	137	366	(669)	(303)
Exceptional items (note 4)	(2)	—	—	—	(2)	6	4
Profit/(loss) before taxation	17	191	19	137	364	(663)	(299)
2003 restated							
Total sales	1,128	1,611	91	205	3,035	1,373	4,408
Inter-segment sales	(85)	(1,569)	(41)	(186)	(1,881)	(308)	(2,189)
Sales to third parties	1,043	42	50	19	1,154	1,065	2,219
Operating profit/(loss) before exceptional items and amortisation	137	152	(5)	(60)	224	(366)	(142)
Amortisation charges	(48)	—	—	—	(48)	—	(48)
Exceptional items (note 4)	(243)	(175)	—	—	(418)	(415)	(833)
Operating profit/(loss)	(154)	(23)	(5)	(60)	(242)	(781)	(1,023)
Share of operating profit – joint ventures	—	26	—	—	26	—	26
— associated undertakings	—	—	—	37	37	—	37
(Loss)/profit on sale of fixed assets (note 6)	—	—	—	(2)	(2)	8	6
Profit/(loss) before interest, taxation and exceptional items	89	178	(5)	(23)	239	(366)	(127)
Exceptional items (note 4)	(243)	(175)	—	(2)	(420)	(407)	(827)
Profit/(loss) before interest and taxation	(154)	3	(5)	(25)	(181)	(773)	(954)
Inter-segment interest (payable)/receivable	(26)	—	—	26	—	—	—
Other (interest payable)/investment income	(23)	(1)	—	19	(5)	(129)	(134)
Profit/(loss) before taxation and exceptionals	40	177	(5)	22	234	(495)	(261)
Exceptional items (note 4)	(243)	(175)	—	(2)	(420)	(407)	(827)
Profit/(loss) before taxation	(203)	2	(5)	20	(186)	(902)	(1,088)

2003 comparatives have been restated to reflect the evolving structure used to manage the Group. Key movements in the year have been the transfer of the Spent Fuel Services business from the Westinghouse Business Group to a separate business segment, and the transfer of the Urenco Limited results from the Westinghouse Business Group to the Corporate business segment. Inter-segment sales for British Nuclear Group have been restated to include the BNFL ALFA fee income of £135 million for the year ended 31 March 2003. Previously this had been classified as other operating income. The key issues underlying these results are explained in the Business Group reviews on pages 22 to 35 and the Financial review on pages 42 to 45.

2. Segmental information continued

a. Business segment analysis continued

	Westinghouse £m	British Nuclear Group £m	Spent Fuel Services £m	Corporate £m	Subtotal £m	BNFL ALFA £m	Total £m
2004							
Intangible assets	634	—	—	—	634	—	634
Tangible assets	353	298	123	58	832	6,342	7,174
Investments:							
Joint ventures	—	32	—	1	33	—	33
Associated undertakings	—	—	—	109	109	—	109
Other	—	—	—	3	3	4,016	4,019
Total fixed assets	987	330	123	171	1,611	10,358	11,969
Customer recoverable relating to nuclear liabilities	5	—	—	—	5	4,889	4,894
Secretary of State's Undertaking	—	—	—	—	—	5,525	5,525
Other net current assets	33	14	5	1,394	1,446	110	1,556
Net current assets	38	14	5	1,394	1,451	10,524	11,975
Nuclear provisions	(349)	(7)	(35)	(17)	(408)	(20,350)	(20,758)
Other provisions	(346)	(147)	(8)	(209)	(710)	(476)	(1,186)
Other long-term liabilities	(368)	(19)	(68)	261	(194)	(4,701)	(4,895)
Total long-term liabilities	(1,063)	(173)	(111)	35	(1,312)	(25,527)	(26,839)
Internal funding	(77)	331	(9)	(245)	—	—	—
Net (liabilities)/assets	(115)	502	8	1,355	1,750	(4,645)	(2,895)
2003 restated							
Intangible assets	768	—	—	—	768	—	768
Tangible assets	380	332	124	63	899	6,588	7,487
Investments:							
Joint ventures	—	32	—	1	33	—	33
Associated undertakings	—	—	—	99	99	—	99
Other	—	—	—	3	3	3,843	3,846
Total fixed assets	1,148	364	124	166	1,802	10,431	12,233
Customer recoverable relating to nuclear liabilities	7	—	—	—	7	4,938	4,945
Secretary of State's Undertaking	—	—	—	—	—	5,159	5,159
Other net current (liabilities)/assets	(116)	(71)	4	1,904	1,721	(713)	1,008
Net current (liabilities)/assets	(109)	(71)	4	1,904	1,728	9,384	11,112
Nuclear provisions	(350)	—	(35)	(17)	(402)	(20,334)	(20,736)
Other provisions	(451)	(312)	(8)	(267)	(1,038)	(261)	(1,299)
Other long-term liabilities	(391)	(23)	(88)	263	(239)	(3,761)	(4,000)
Total long-term liabilities	(1,192)	(335)	(131)	(21)	(1,679)	(24,356)	(26,035)
Internal funding	33	258	(4)	(287)	—	—	—
Net (liabilities)/assets	(120)	216	(7)	1,762	1,851	(4,541)	(2,690)

Notes to the accounts continued**2. Segmental information continued****b. Geographical segment analysis**

	EU (excluding UK) £m	Europe Other £m	Japan and Far East £m	North and South America £m	UK £m	Total £m
2004						
Turnover by destination						
Sales to third parties	258	59	369	682	954	2,322
Turnover by origin						
Total sales	208	3	3	733	1,393	2,340
Inter-segment sales	—	—	(3)	(10)	(5)	(18)
Sales to third parties	208	3	—	723	1,388	2,322
Profit/(loss) before taxation by origin						
Operations before exceptional items	42	—	1	(19)	(327)	(303)
Exceptional items	—	—	—	—	4	4
Total	42	—	1	(19)	(323)	(299)
Net assets/(liabilities)	243	—	—	747	(3,885)	(2,895)
2003						
Turnover by destination						
Sales to third parties	252	53	422	671	821	2,219
Turnover by origin						
Total sales	192	6	3	747	1,296	2,244
Inter-segment sales	—	—	(3)	(10)	(12)	(25)
Sales to third parties	192	6	—	737	1,284	2,219
Profit/(loss) before taxation by origin						
Operations before exceptional items	27	2	—	59	(349)	(261)
Exceptional items	—	—	—	(188)	(639)	(827)
Total	27	2	—	(129)	(988)	(1,088)
Net assets/(liabilities)	201	—	—	789	(3,680)	(2,690)

3. Net operating costs and expenses

	2004	2003		
	Total before and after exceptional items £m	Total before exceptional items £m	Exceptional items £m	Total £m
Employee costs (note 5)	1,035	987	—	987
Nuclear provisions charge	85	21	415	436
Other provisions charge	252	93	251	344
Depreciation — on capitalised decommissioning costs	47	115	—	115
— provisions for impairment	81	81	167	248
— other depreciation	382	363	—	363
Amortisation of goodwill	43	48	—	48
Raw materials and consumables	537	508	—	508
Research and development charges not directly recoverable from customers	59	67	—	67
Other income and operating charges	208	200	—	200
Operating lease rentals	5	8	—	8
Own work capitalised	(45)	(67)	—	(67)
Own work on nuclear fuel stock	(14)	(14)	—	(14)
Regional development grants released	(2)	(1)	—	(1)
	2,673	2,409	833	3,242

Auditors' remuneration

It is the Group's policy to engage the Group's auditors, Ernst & Young LLP, on assignments where their expertise and experience with the Group are important or where they win work on a competitive basis. The fees are included in other income and operating charges and are analysed below in line with recommended best practice. Comparatives have been restated for consistency, to include audit-related assurance work, previously classified as further assurance work within annual audit fees and, to reclassify non-audit fees into the relevant categories in line with the latest guidance.

Annual audit fees

	Group		Company	
	2004 £000	2003 £000	2004 £000	2003 £000
Statutory audit	1,504	1,502	556	405
Audit related reporting	224	315	174	160
Total annual audit fees	1,728	1,817	730	565

Other non-audit fees

	Group	
	2004 £000	2003 £000
Further assurance services	243	319
Taxation advice	329	359
	572	678

Notes to the accounts continued

4. Exceptional items

	2004 £m	2003 £m
Magnox station decommissioning provisions	—	(415)
Springfields impairment and provisions	—	(230)
Restructuring provisions	—	(13)
Contract losses in US	—	(175)
Decrease in operating profit	—	(833)
Profit on sale of fixed assets (note 6)	4	6
Increase/(decrease) in profit before taxation	4	(827)

Magnox station decommissioning provisions

The 2003 Annual Report and Accounts noted that an exercise was underway to prepare new baseline decommissioning plans (BDPs) for the pre-care and maintenance phase of the decommissioning of the Magnox sites. During 2002-2003 new plans for Hinkley and Bradwell sites were completed, cost estimates were prepared based on the Group's current strategy for performing such work and, as a result, nuclear provisions were increased by £415 million. The accounts further disclosed that this process of preparing BDPs would be completed over the following three years dealing with the remaining nine sites. During 2003-2004 new plans for Hunterston A, Trawsfynydd and Berkeley were drawn up, which, in the normal course of events, would have been incorporated into the accounts.

In preparation for the establishment of the NDA and associated restructuring expected in April 2005, the Group continues to prepare full lifetime LCBLs. These will form the operational basis of actually discharging liabilities from 1 April 2005 when the NDA takes responsibility for the sites. The work we have done in producing the first draft version of the LCBLs and understanding better the expectations of the precursor organisation of the NDA has caused us fundamentally to challenge our existing strategies and assumptions (on which the BDPs were based) for the early period of decommissioning in terms of both cost and time to complete the work. Whilst producing the BDPs continues to be a necessary part of the process for preparing the LCBLs, given that they, for example, include preparing a detailed engineering inventory of each site, the Board has however formed the view that the current provisions remain their current best estimate of reactor decommissioning provisions. The challenges to the strategy will continue to be evaluated over the course of the coming financial year. In the meantime it is considered appropriate to retain the £415 million increase in provisions recorded last year, although this may prove to be attributable to sites on a different basis to that originally anticipated. Further details on nuclear provisions are included in note 24.

British Energy

Last year the announcement by our major customer, British Energy (BE), that it had initiated discussions with Her Majesty's Government (HMG) with a view to seeking immediate financial support, and the subsequent revision to the contracts between the Group and BE, resulted in an impairment of assets and increase in provisions at our Springfields site. Subsequent to the announcement, the Group has worked with BE, as have all of BE's significant creditors and bondholders, to put into practice a solvent restructuring plan which seeks to enable BE to continue trading and restore its financial standing. Such work culminated in the execution of a Creditors' Restructuring Agreement in October 2003, creating a financial background for BE to continue trading up to and, hopefully, beyond EU clearance of HMG's proposed state aid package. It is anticipated that the EU Competition Commission will rule in connection with HMG's application for state aid clearance in mid to late 2004. If this ruling is positive, BNFL and BE will enter a new phase of contractual arrangements with BE being responsible for the payment of spent fuel management services for any fuel loaded into their AGR stations on or after the date of state aid clearance. Financial responsibility for the management of spent fuel by BNFL loaded into BE's AGR stations prior to this date will be met by HMG under a Historic Liabilities Funding Agreement. BE will remain responsible for all payments in respect of AGR fuel fabrication for which payments will be discounted on a variable basis dependent upon a formula tied to the outturn electricity price per megawatt hour in the UK, such discount is capped at a maximum of £15 million per annum.

Contract losses in the US

Last year a £175 million exceptional charge was reported to reflect increased costs on two fixed price contracts in the US. There are no further exceptional charges on the contracts this year.

5. Employee information

	2004	2003 Restated
Average number of employees		
Westinghouse	7,665	8,044
British Nuclear Group	13,688	13,129
Spent Fuel Services	494	501
Corporate	1,270	1,273
BNFL ALFA	32	24
	23,149	22,971
	£m	£m
Employee costs		
Wages and salaries	867	834
Social security costs	74	67
Other pension costs	40	35
Other employee costs	54	51
	1,035	987

The figures given above include company executive directors. Further details of directors' emoluments are set out in Tables A to C within the Remuneration report on pages 52 and 53.

6. Profit on sale of fixed assets

	2004 £m	2003 £m
Tangible fixed assets	(1)	(5)
Realised gains on Nuclear Liabilities Investment Portfolio	5	11
	4	6

7. Investment and interest income

	2004 £m	2003 £m
Nuclear Liabilities Investment Portfolio:		
Amortisation of premium/discount	(16)	13
Indexation of gilts	36	61
Investment income	161	142
Interest receivable from Secretary of State's Undertaking	366	375
Income from current asset investments	80	88
Reversal of previously recognised losses on investments held by Captive Insurance Subsidiaries	61	—
Exchange gains	—	43
Interest receivable relating to loans to joint ventures	1	1
	689	723
Financing income from long-term contract advance payments reclassified to turnover	(37)	(40)
	652	683

Income from the Nuclear Liabilities Investment Portfolio and the contractually agreed interest on the Secretary of State's Undertaking is available to set off against the increase in nuclear liabilities arising from changes in price levels and the unwinding of one year's discounting known as revaluation. Over time the income generated should match the time-related increases in nuclear liabilities included under interest payable and similar charges.

Notes to the accounts continued

8. Interest payable and similar charges

	2004 £m	2003 £m
Revalorisation on nuclear provisions		
Changes in price levels	314	393
Unwinding of one year's discount	313	300
	627	693
Revalorisation on other provisions		
Changes in price levels	13	13
Unwinding of one year's discount	12	10
	25	23
Total revalorisation	652	716
Interest payable:		
Interest on loans	9	19
Exchange losses	2	—
Bank charges	3	2
Share of associated undertakings' interest payable	6	6
Total interest payable	20	27
Unrealised losses on investments held by Captive Insurance Subsidiaries	—	74
	672	817

9. Taxation on (loss)/profit on ordinary activities

a. Analysis of taxation credit in the year

	2004 Total before and after exceptional items £m	Total before exceptional items £m	Exceptional items £m	2003 Total £m
UK corporation taxation in respect of parent and subsidiaries:				
Adjustment in respect of prior years	61	43	—	43
	61	43	—	43
Joint ventures' taxation charge	(2)	(8)	—	(8)
Associated undertakings' taxation charge	(14)	(15)	—	(15)
	45	20	—	20
Overseas taxation charge	(3)	(7)	—	(7)
Total current taxation credit	42	13	—	13
Deferred taxation in respect of parent and subsidiaries (current year)	63	139	71	210
Taxation credit	105	152	71	223

9. Taxation on (loss)/profit on ordinary activities continued**b. Factors affecting taxation credit for the year**

The taxation assessed on the loss on ordinary activities for the year is different from the standard rate of UK corporation taxation of 30%. The differences are reconciled below:

	2004 £m	2003 £m
Loss on ordinary activities before taxation	(299)	(1,088)
Loss on ordinary activities before taxation multiplied by the standard rate of corporation taxation in the UK of 30% (2003: 30%)	90	326
Effects of:		
Expenses not deductible for taxation purposes	(13)	(24)
Capital allowances in excess of depreciation	(62)	(121)
Other timing differences	(50)	(138)
Adjustments in respect of prior years	61	43
Associated undertakings and joint venture taxation	(6)	(5)
Overseas taxation	22	(68)
Current taxation credit for period (note 9a)	42	13

10. Intangible fixed assets

	Goodwill £m	Licences £m	Total £m
Cost at 1 April 2003	931	3	934
Exchange adjustments	(116)	—	(116)
Additions	2	—	2
Cost at 31 March 2004	817	3	820
Amortisation at 1 April 2003	163	3	166
Exchange adjustments	(23)	—	(23)
Charge for the year	43	—	43
Amortisation at 31 March 2004	183	3	186
Net book value at 31 March 2004	634	—	634
Net book value at 31 March 2003	768	—	768

The goodwill above arose on the acquisition of ABB's commercial nuclear power business on 28 April 2000 and the acquisition of Westinghouse Electric Company LLC on 22 March 1999.

Notes to the accounts continued

11. Tangible fixed assets

a. Group

	Land and buildings		Plant and machinery		Fixtures, fittings, tools and equipment £m	Assets in course of construction £m	Total £m
	Long leasehold £m	Freehold £m	Capitalised decommissioning costs (note 1f) £m	Other £m			
Cost at 1 April 2003	5	3,591	3,340	4,548	170	1,747	13,401
Exchange adjustments	—	(12)	(3)	(27)	(2)	(46)	(90)
Additions	1	2	203	25	5	269	505
Disposals	—	(16)	(282)	(29)	(5)	—	(332)
Assets in course of construction commissioned	—	15	—	125	12	(152)	—
Cost at 31 March 2004	6	3,580	3,258	4,642	180	1,818	13,484
Depreciation at 1 April 2003	1	1,671	1,040	2,942	141	119	5,914
Exchange adjustments	—	(4)	(1)	(13)	(1)	—	(19)
Impairment of assets	—	7	—	21	5	48	81
Charge for the year	2	149	47	217	14	—	429
Disposals	—	(10)	(52)	(29)	(4)	—	(95)
Depreciation at 31 March 2004	3	1,813	1,034	3,138	155	167	6,310
Net book value at 31 March 2004	3	1,767	2,224	1,504	25	1,651	7,174
Net book value at 31 March 2003	4	1,920	2,300	1,606	29	1,628	7,487

b. Company

	Plant and machinery					
	Freehold land and buildings £m	Capitalised decommissioning costs (note 1f) £m	Other £m	Fixtures, fittings, tools and equipment £m	Assets in course of construction £m	Total £m
Cost at 1 April 2003	3,419	4,444	3,863	108	1,283	13,117
Additions	—	322	21	5	162	510
Disposals	(9)	(286)	(28)	(4)	—	(327)
Assets in course of construction commissioned	5	—	83	5	(93)	—
Cost at 31 March 2004	3,415	4,480	3,939	114	1,352	13,300
Depreciation at 1 April 2003	1,593	638	2,476	90	14	4,811
Impairment of assets	—	—	7	—	4	11
Charge for the year	144	44	186	11	—	385
Disposals	(9)	(25)	(28)	(3)	—	(65)
Depreciation at 31 March 2004	1,728	657	2,641	98	18	5,142
Net book value at 31 March 2004	1,687	3,823	1,298	16	1,334	8,158
Net book value at 31 March 2003	1,826	3,806	1,387	18	1,269	8,306

The company's impairment charge represents a write down of capital expenditure in the year on tangible fixed assets at our Springfields site that were fully impaired last year. The Group's impairment charge also includes impairment of capital expenditure on Magnox stations, which were impaired in the year ended 31 March 2002.

Freehold land, amounting to £5 million (2003: £5 million) for the Group and £5 million (2003: £5 million) for the company, has not been depreciated.

Notes to the accounts

12. Fixed assets – investments

a. Summary

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
Subsidiary undertakings (note 12b)	–	–	1,131	1,136
Joint ventures (note 12c)	33	33	2	2
Associated undertakings (note 12d)	109	99	–	–
Trade investments (note 12e)	3	3	2	2
Nuclear Liabilities Investment Portfolio (note 12f)	4,016	3,843	4,040	3,869
	4,161	3,978	5,175	5,009

See page 98 for details of principal subsidiary undertakings, associated undertakings and joint ventures.

b. Subsidiary undertakings

	Shares £m	Loans £m	Total cost £m	Company	
				Amounts provided £m	Net book value £m
At 1 April 2003	1,087	73	1,160	(24)	1,136
Exchange movements	–	(2)	(2)	–	(2)
Repayments	–	(3)	(3)	–	(3)
At 31 March 2004	1,087	68	1,155	(24)	1,131

c. Joint ventures

	Share of net assets £m	Goodwill £m	Loans and advances £m	Group	Shares £m	Loans and advances £m	Company
				Total £m			Total £m
Cost at 1 April 2003	13	24	88	125	1	63	64
Share of retained profit and reserves	5	–	–	5	–	–	–
Reclassifications	(20)	20	–	–	–	–	–
Cost at 31 March 2004	(2)	44	88	130	1	63	64
Amounts amortised/provided at 1 April 2003	–	5	87	92	–	62	62
Amortisation charge in the year	–	5	–	5	–	–	–
Amounts amortised/provided at 31 March 2004	–	10	87	97	–	62	62
Net book value at 31 March 2004	(2)	34	1	33	1	1	2
Net book value at 31 March 2003	13	19	1	33	1	1	2

The principal joint ventures are Westinghouse Government Environmental Services Company LLC, Westinghouse Government Services Company LLC, United Kingdom Nirex Limited and AWE Management Limited.

Loans of £87 million for the Group (2003: £87 million) and £62 million for the company (2003: £62 million) have been made to United Kingdom Nirex Limited to fund development expenditure for building an intermediate-level nuclear waste repository. Full provision has been made against these loans.

Notes to the accounts continued

12. Fixed assets – investments continued

d. Associated undertakings

	Group share of net assets £m
Net book value at 1 April 2003	99
Exchange adjustment	(4)
Share of retained profit and reserves	14
Net book value at 31 March 2004	109

The principal associated undertaking is Urenco Limited. During the year, as part of a restructuring of the Urenco business, in which the Group holds one-third of the shares, the Group subscribed for a shareholding in a newly formed Urenco subsidiary, Enrichment Technology Company Limited (ETC). As this transaction has not resulted in any change in the Group's effective interest in its associated undertakings, no additions are shown in the table above.

The Group has entered into a conditional contract with Société de Participations du Commissariat à l'énergie atomique (trading as Areva) to sell 50% of its interest in ETC. As part of these arrangements, a refundable deposit of €50 million (£35 million) has been received in the year and is included in other creditors (note 18) as at 31 March 2004. The transaction should be completed in the next financial year, subject to the necessary governmental and competition clearances being granted.

e. Trade investments

	Group			Company		
	Cost £m	Amounts provided £m	Net book value £m	Cost £m	Amounts provided £m	Net book value £m
Balance at 1 April 2003 and at 31 March 2004	11	(8)	3	9	(7)	2

f. Nuclear Liabilities Investment Portfolio

The Nuclear Liabilities Investment Portfolio (NLIP) represents funds earmarked for the costs associated with the discharge of nuclear liabilities. An analysis of movements in the portfolio is shown below. As can be seen from this analysis there has been no drawdown from the fund in the current financial year, all liabilities expenditure in the year has been funded by cash generated from operations.

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
Balance at 1 April	3,843	4,023	3,869	4,050
Profit on sale of investments	5	11	5	11
Investment income	148	135	148	135
Amortisation of premium/discount	(16)	13	(18)	12
Indexation of gilts	36	61	36	61
Total liabilities discharged (note 25c)	(510)	(469)	(510)	(469)
Less liabilities funded by operations	510	69	510	69
Balance at 31 March	4,016	3,843	4,040	3,869

In order to ensure that funds are available when needed to meet the long-term nuclear liabilities, the investment policy has to address long-term returns and their relationship to inflation, the effects of taxation, credit risk and reinvestment risk. The fund is thus invested in a combination of a gilts investment portfolio, which generally holds gilts to maturity and, an actively traded managed portfolio, invested through fund managers.

12. Fixed assets – investments continued**f. Nuclear Liabilities Investment Portfolio continued****i. Gilts investment portfolio**

The Group has invested £1,375 million of the portfolio in index-linked gilts and £982 million in conventional gilts, with the remaining £101 million held as bank deposits. The gilts are intended to be held until redemption. The index-linked gilts have an average period to maturity of 14.62 years and returned 2.33% per annum after taxation and inflation in the year. The advantages of this instrument to the portfolio are taxation-free indexation cover for inflation, a roughly constant annual post-taxation real yield to maturity and excellent credit risk. There are two areas of risk associated with this instrument: firstly the taxation legislation may change; and secondly, given the longest maturity is up to 2024, but the nuclear liabilities go out to 2150, there will be a significant degree of refinancing risk if the Government does not issue longer maturing index-linked gilts in due course.

ii. Managed portfolio

£1,558 million is invested through fund managers, against either a LIBID or index-linked benchmark dependent upon the maturity profile of the investment. Funds are primarily invested in fixed income instruments, such as certificates of deposit, index-linked and conventional gilts and a very small proportion in equity investments. The purpose of using fund managers is to provide some flexibility and add value by active strategic investment. Performance is monitored through monthly reports and regular meetings. The potential change in value on the funds is controlled by the benchmarks and by maturity limits. Credit risk on non-gilt investments is controlled by limiting the amount that can be placed with each counterparty and specifying a minimum creditworthiness of the counterparty as determined by the rating agencies.

A summary of the movements in the individual portfolios is as follows:

	Group			Company		
	Gilts investment portfolio £m	Managed portfolio £m	Total £m	Gilts investment portfolio £m	Managed portfolio £m	Total £m
Balance at 1 April 2003	2,348	1,495	3,843	2,374	1,495	3,869
Additions	797	4,862	5,659	797	4,862	5,659
Disposals	(707)	(4,799)	(5,506)	(707)	(4,799)	(5,506)
Amortisation of premium/discount	(16)	—	(16)	(18)	—	(18)
Indexation of gilts	36	—	36	36	—	36
Balance at 31 March 2004	2,458	1,558	4,016	2,482	1,558	4,040

The NLIP contains listed and unlisted investments as follows:

	Group				Company			
	2004		2003		2004		2003	
	Market value £m	Book value £m	Market value £m	Book value £m	Market value £m	Book value £m	Market value £m	Book value £m
Listed investments	4,136	3,899	4,059	3,824	4,136	3,923	4,059	3,850
Unlisted investments	117	117	19	19	117	117	19	19
Total	4,253	4,016	4,078	3,843	4,253	4,040	4,078	3,869

The value of listed investments in the company is greater than that of the Group due to the transfer of investments from Magnox Electric plc at the then market value, being in excess of cost, following the acquisition of that company in the year ended 31 March 1998. Unlisted investments are principally bank deposits.

Notes to the accounts continued**13. Stocks**

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
Nuclear fuel	19	22	2	5
Raw materials and consumables	391	350	39	40
Work in progress	73	74	35	34
Finished goods	34	18	4	3
	517	464	80	82

14. Debtors falling due within one year**a. Summary**

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
Trade debtors	204	264	85	140
Recoverable on long-term contracts	73	81	—	—
VAT	38	33	24	21
Corporation taxation	1	11	1	11
Prepayments and accrued income	283	187	241	89
Other debtors	75	17	66	12
Owed by Group undertakings	—	—	1,600	1,794
Owed by associated undertakings	9	9	—	—
Customer recoverable relating to nuclear liabilities (note 15)	263	210	595	637
	946	812	2,612	2,704

b. Amounts outstanding from employees

	Group		Company	
	Number of employees	£000	Number of employees	£000
As at 31 March 2004	91	558	84	512
As at 31 March 2003	77	639	77	639

15. Customer recoverable relating to nuclear liabilities

The Group and company have commercial agreements in place under which some or all of the expenditure required to settle nuclear liabilities will be recovered from third parties. The movements in amounts recoverable during the year are detailed in the table below. Revalorisation reflects the changes in price levels in the year and the unwinding of one year's discounting.

	Decommissioning fixed assets £m	Decommissioning debtor £m	Waste management debtor £m	Reprocessing debtor £m	Total debtors £m	Total recoverable £m
Group						
Balance at 1 April 2003	2,128	77	4,868	—	4,945	7,073
Revalorisation	107	4	183	—	187	294
(Decrease)/increase in the year	(126)	(13)	17	—	4	(122)
Discharge of liabilities	(29)	—	(242)	—	(242)	(271)
Balance at 31 March 2004	2,080	68	4,826	—	4,894	6,974
Company						
Balance at 1 April 2003	3,679	161	8,587	911	9,659	13,338
Revalorisation	185	8	336	43	387	572
(Decrease)/increase in the year	(106)	3	712	154	869	763
Discharge of liabilities	(45)	—	(423)	(108)	(531)	(576)
Balance at 31 March 2004	3,713	172	9,212	1,000	10,384	14,097

The debtors balance is recoverable as follows:

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
Amounts falling due within one year	263	210	595	637
Amounts falling due after more than one year	4,631	4,735	9,789	9,022
	4,894	4,945	10,384	9,659

Notes to the accounts continued

16. Secretary of State's Undertaking (due after more than one year)

	Group £m
Balance at 1 April 2003	5,159
Interest accrued during the year	366
Balance at 31 March 2004	5,525

The Secretary of State's Undertaking is an agreement between Her Majesty's Secretary of State for Trade and Industry and Magnox Electric plc. The Secretary of State has undertaken to pay Magnox Electric plc £3,700 million (March 1998 money values) together with interest at a rate of 4.5% per annum above inflation (based on RPI) on the outstanding amount. Payments commence in the year ending 31 March 2008 and cease in the year ending 31 March 2116. The terms of the Undertaking provide for potential adjustments to the outstanding amount in two circumstances:

- a. Where actions taken by persons or bodies external to the BNFL Group cause or may cause a reassessment of the nuclear related liabilities of the Group attributable to the Magnox fuel cycle (Magnox liabilities). Magnox liabilities account for over 80% of the Group's nuclear liabilities.
- b. Where there is an adjustment to provisions as a result of downward revisions in the estimate of the cost of Magnox liabilities for reasons other than those covered by (a) above.

The next review by Her Majesty's Government in relation to (a) above was due on 1 April 2003. Given the progress being made to implement the proposals on the restructuring of UK civil nuclear liabilities set out in the Ministerial statement made in the House of Commons on 28 November 2001, a deferral of this review has been agreed.

Reductions in provisions falling within (b) above are to be shared between the Group and the Secretary of State (via adjustment of the outstanding amount of the Undertaking) on a sliding scale with the maximum reduction in the Undertaking being £800 million escalated by 2.5% above inflation from 1 April 1998. The directors have not assumed any increase in the Undertaking for the revisions to nuclear liabilities estimates in recent years.

17. Current asset investments and short-term deposits

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
Gilt investments – medium-term maturity	105	112	105	112
– short-term maturity	123	123	123	123
Managed investments	608	548	–	–
Short-term deposits	686	1,039	593	911
	1,522	1,822	821	1,146

Gilt investments

The Group has invested £105 million in index-linked gilts, which are intended to be held until redemption. These funds are earmarked to cover decommissioning costs at our Springfields site. These have an average maturity of 20.01 years and returned 3.12% per annum after taxation and inflation this year. The advantages and risks of this type of instrument are discussed in the NLIP note 12f. During the year some of the gilts were redeemed on maturity, with the resulting cash inflow used to cover associated liabilities expenditure. A further £123 million has been invested in conventional gilts which are due to mature in December 2005.

Managed investments

Managed investments of £608 million represent funds held by Captive Insurance Subsidiaries. Funds are invested via a number of fund managers, who operate portfolios which include a combination of equity investments, fixed income instruments and bank deposits. There has been a significant increase in the value of the funds in the year as a result of the recovery in the market value of equities from 31 March 2003.

17. Current asset investments and short-term deposits continued**Short-term deposits**

These consist of bank deposits and other fixed and call deposits, supported by a level of funds invested in certificates of deposit and a money fund to cover unforeseen requirements. Liquidity is managed by preparing short and medium-term cash flow forecasts against which the maturity of bank deposits is timed. An element of the short-term deposits, £91 million, as at 31 March 2004 is held within charge over deposit accounts, over which customers have a legal charge, as explained in note 33.

Current asset investments and short-term deposits include listed and unlisted investments as follows:

	Group				Company			
	2004		2003		2004		2003	
	Market value £m	Book value £m	Market value £m	Book value £m	Market value £m	Book value £m	Market value £m	Book value £m
Listed investments:								
Carried at market value	583	583	548	548	—	—	—	—
Carried at cost	244	228	258	235	244	228	258	235
Total listed investments	827	811	806	783	244	228	258	235
Unlisted investments	711	711	1,039	1,039	593	593	911	911
Total	1,538	1,522	1,845	1,822	837	821	1,169	1,146

The historic cost of the listed investments carried at market value was £592 million (2003: £616 million).

18. Creditors: amounts falling due within one year

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
Loans (note 20)	27	30	—	—
Bank overdraft	9	3	278	185
Payments received on account (note 21)	683	1,548	835	1,722
Obligations under finance leases and hire purchase contracts	2	3	—	—
Trade creditors	182	176	72	62
VAT	38	41	21	28
Corporation taxation	10	43	6	4
Other taxes and social security	18	15	14	10
Accruals and deferred income	418	325	221	142
Other creditors	39	9	2	3
Owed to Group undertakings	—	—	1,457	2,217
	1,426	2,193	2,906	4,373

Accruals and deferred income in both the Group and company include £64 million (2003: £nil) relating to the depreciation matching accrual (note 1h) and £1 million (2003: £1 million) relating to capital grants (note 1h). Included within other creditors is a refundable deposit of £35 million relating to the Group's conditional contract for the sale of 50% of the Group's interest in ETC (note 12d).

Notes to the accounts continued

19. Creditors: amounts falling due after more than one year

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
Loans (note 20)	—	21	—	—
Payments received on account (note 21)	4,304	3,375	5,667	4,793
Accruals and deferred income	579	587	579	587
Other	12	17	2	2
	4,895	4,000	6,248	5,382

Accruals and deferred income in both the Group and company include £571 million (2003: £578 million) relating to the depreciation matching accrual (note 1h) and £8 million (2003: £9 million) relating to capital grants (note 1h).

20. Loans

	Group	
	2004 £m	2003 £m
Repayable – in one year or less, or on demand	27	30
– in more than two years but not more than five years	—	21
	27	51

Loans are secured by Parent company guarantees.

21. Payments received on account

Payments on account have been received from customers for the provision of services under long-term contracts. These will be released to the profit and loss account, and hence turnover recognised, as the services are provided. The expected profile for release of payments received on account as at 31 March is as follows:

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
In one year or less	683	1,548	835	1,722
In more than one year but not more than two years	488	611	861	946
In more than two years but not more than five years	1,542	1,650	2,741	2,930
In more than five years	2,274	1,114	2,065	917
	4,987	4,923	6,502	6,515

22. Undrawn committed borrowing facilities

The Group has undrawn committed borrowing facilities of £70 million which expire within two to five years (2003: £83 million within two to five years).

23. Provisions for liabilities and charges

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
Nuclear provisions – recoverable under commercial agreement (note 24)	6,974	7,073	14,097	13,338
– Group funded (note 24)	13,784	13,663	2,360	2,237
Nuclear provisions total	20,758	20,736	16,457	15,575
Deferred taxation (note 26)	147	210	–	–
Other provisions (note 27)	1,039	1,089	954	869
	21,944	22,035	17,411	16,444

24. Nuclear provisions**a. Summary of the movements in nuclear provisions**

	Decommissioning		Waste management		Reprocessing		Total	
	Recoverable under commercial agreement £m	Group funded £m	Recoverable under commercial agreement £m	Group funded £m	Recoverable under commercial agreement £m	Group funded £m	Recoverable under commercial agreement £m	Group funded £m
Group								
Balance at 1 April 2003	2,205	5,879	4,868	6,601	–	1,183	7,073	13,663
Exchange adjustments	–	(13)	–	–	–	–	–	(13)
Reclassifications	–	30	–	(31)	–	7	–	6
Revalorisation	111	291	183	283	–	53	294	627
(Decrease)/increase in the year	(139)	10	17	44	–	51	(122)	105
Discharge of liabilities	(29)	(177)	(242)	(303)	–	(124)	(271)	(604)
Balance at 31 March 2004	2,148	6,020	4,826	6,594	–	1,170	6,974	13,784
Company								
Balance at 1 April 2003	3,840	1,132	8,587	988	911	117	13,338	2,237
Reclassifications	–	30	–	(31)	–	7	–	6
Revalorisation	193	59	336	40	43	6	572	105
(Decrease)/increase in the year	(103)	41	712	43	154	21	763	105
Discharge of liabilities	(45)	(37)	(423)	(38)	(108)	(18)	(576)	(93)
Balance at 31 March 2004	3,885	1,225	9,212	1,002	1,000	133	14,097	2,360

The Group has estimated the financial cost of meeting its obligations to decommission radioactive facilities and has provided for them. These obligations address the demolition of plants used for fuel manufacture, reprocessing operations and generating plant together with the disposal of associated waste. Provisions are also made for the treatment, handling and disposal of waste products arising from reprocessing operations together with defuelling, reprocessing and waste management of used nuclear fuel from the Group's reactors. The bulk of these provisions relate to treatment plant and related facilities at Sellafield, where the complexity and number of plants is significantly greater than at the other locations for which the Group has site licence responsibility.

Notes to the accounts continued**24. Nuclear provisions continued****a. Summary of the movements in nuclear provisions continued**

For safety reasons, much of the dismantling and demolition work will not occur for a considerable time. Similarly, the costs of constructing long-term storage for waste will not be incurred for a long time, and the accounting provisions for such costs must necessarily be based on estimates, which are calculated using the practical experience and extensive knowledge that already exists.

In respect of historic wastes, specifically those arising from the early military and civil nuclear programmes, following extensive work over a number of years, the Board approved a substantially revised retrieval and processing strategy in the financial year ending 31 March 2002. Despite the extensive work undertaken, the nature of the wastes, the length of time for which they have been stored and the age of the storage facilities mean that much further work will be required over a number of years to confirm and further refine this strategy. The Board has recorded its best estimate of the related liabilities based on available knowledge. The Group's procedures would normally require this estimate to include risk, which in this context means the financial implications of a range of possible alternative outcomes associated with the treatment of these wastes. In this case however, the level of uncertainty associated with these alternatives is such that the Board has been unable to quantify this incremental financial impact with reasonable certainty. As a consequence, it is likely that the liabilities will differ from the amounts recorded although those amounts remain the best available estimate at the present time. As indicated in note 4, the station decommissioning costs are under review.

The estimates on which all the provisions are based are themselves reliant upon assumptions derived from detailed technical assessments of the processes and methods likely to be used to discharge the obligations. These assumptions reflect a combination of latest technical knowledge available, the timescale involved before the work is carried out and the requirements of the existing regulatory regime and commercial agreements, in addition to statistical modelling of the financial impact of the various outcomes. The nature of the obligations however means that fundamental uncertainties remain regarding the measurement of the liabilities and the timing of the cash flows. Until the new structure announced by Her Majesty's Government is established and responsibility for these liabilities transferred, the impact of any additional liabilities could materially affect the results of operations and financial condition of the Group. Further background to nuclear liabilities is provided on pages 95 to 97.

b. Funding of long-term nuclear provisions

The following table shows the cash element of the Group funded provision and the percentage covered by funds held by the Group as at the balance sheet date:

	2004 £m	2003 £m
Group funded provisions	13,784	13,663
Non-cash (see below)	(968)	(941)
Future cash expenditure in respect of existing liabilities	12,816	12,722
Nuclear Liabilities Investment Portfolio market value (note 12f)	4,253	4,078
Secretary of State's Undertaking in relation to the liabilities of Magnox Electric plc (note 16)	5,525	5,159
Funds earmarked for liabilities	9,778	9,237
Level of percentage funding	76%	73%

The non-cash adjustment represents depreciation on certain historic capital expenditure, which will be charged against provisions over the remaining operating life of those assets.

25. Nuclear liabilities**a. Total future cash expenditure**

The following table shows the current estimate of total lifetime future cash expenditure and the proportion funded by the Group. The provisions as disclosed in the balance sheet are discounted at 2.5% per annum. The table below indicates both the discounted and undiscounted future cash expenditure.

	Total future cash expenditure		Group funded future cash expenditure	
	Undiscounted £m	Discounted £m	Undiscounted £m	Discounted £m
Decommissioning	18,542	8,112	14,109	5,978
Waste management	20,032	10,144	12,592	6,010
Reprocessing	2,787	2,251	1,630	1,305
At 31 March 2004	41,361	20,507	28,331	13,293
At 31 March 2003	41,265	20,733	27,865	13,372

b. Reconciliation of Group funded provision to Group-funded future cash expenditure

	2004 £m	2003 £m
Group funded provisions	13,784	13,663
Non-cash	(968)	(941)
Future activities for which provision is not yet required (see below)	477	650
Group funded future cash expenditure	13,293	13,372

Future activities for which provision is not yet required relates to liabilities expenditure which is not yet provided, as the recognition criteria under FRS 12 have not yet been met.

c. Movements in future cash expenditure

	Total future cash expenditure		Group funded future cash expenditure	
	Undiscounted £m	Discounted £m	Undiscounted £m	Discounted £m
Balance at 1 April 2003	41,265	20,733	27,865	13,372
Revalorisation	1,099	1,025	742	660
Discharged in year	(813)	(813)	(510)	(510)
Other changes	(190)	(438)	234	(229)
Balance at 31 March 2004	41,361	20,507	28,331	13,293

d. Projected profile of future cash expenditure

The projected cash expenditure profile over the next 150 years is as shown below:

Years	Liabilities discharged	Cash expenditure £bn
2004 to 2014	Construction and operation of waste management facilities, together with some reprocessing and decommissioning	12
2015 to 2065	Decommissioning the Group's nuclear facilities and waste management activities including waste disposal	14
2066 to 2150	Final stages of decommissioning the Group's nuclear facilities, together with costs associated with the construction and operation of a deep waste repository	15
		41

Notes to the accounts continued

26. Deferred taxation

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
Capital allowances in advance of depreciation	436	500	424	486
Other timing differences	(289)	(290)	(424)	(486)
	147	210	—	—

The movement in the year relates to a current year deferred taxation credit to the profit and loss account of £63 million (company: Enil). Other timing differences relate principally to nuclear provisions.

There is considerable uncertainty regarding the current and total taxation charges or credits in future periods due to Government proposals to restructure the Group as part of the formation of the NDA. At this time however the Group continues to provide for deferred taxation on a basis which is consistent with prior periods.

The Group has an unrecognised deferred taxation asset amounting to £1,079 million (2003: £801 million) consisting of fixed asset timing differences of £109 million (2003: £161 million), other timing differences of £675 million (2003: £333 million) and losses of £295 million (2003: £307 million). The unrecognised deferred taxation asset arises both in the wholly owned subsidiary undertaking Magnox Electric plc, where no benefit is expected to crystallise in the future and also on non-trading losses.

The unrecognised deferred taxation asset is unable to be offset against the deferred taxation liability as the asset arises in one legal entity, whilst the liability is in a separate legal entity.

27. Other provisions

	Contract settlements (a) £m	Decommissioning contract pensions (b) £m	Other contract provisions (b) £m	Restructuring and pension costs (c) £m	Other provisions (d) £m	Total £m
Group						
Balance at 1 April 2003	192	181	324	278	114	1,089
Exchange adjustments	(31)	(25)	(1)	(6)	(8)	(71)
Revaluation	7	—	9	9	—	25
Reclassifications	—	21	—	(6)	(21)	(6)
Charge in the year	—	2	187	46	17	252
Released in the year	(6)	(18)	(9)	(1)	(1)	(35)
Expenditure in the year	(36)	(57)	(42)	(71)	(9)	(215)
Balance at 31 March 2004	126	104	468	249	92	1,039
Company						
Balance at 1 April 2003	—	—	253	183	433	869
Revaluation	—	—	8	9	—	17
Reclassifications	—	—	—	(6)	—	(6)
Charge in the year	—	—	179	22	9	210
Released in the year	—	—	(10)	(1)	(78)	(89)
Expenditure in the year	—	—	(20)	(26)	(1)	(47)
Balance at 31 March 2004	—	—	410	181	363	954

27. Other provisions continued

a. Contract settlements

The Westinghouse Business Group has existing obligations in respect of steam generator and uranium supply contract settlements totalling £126 million (2003: £192 million).

The provision for steam generator supply contracts relates to the settlement of various claims brought by US utilities, claiming damages in connection with alleged tube degradation in steam generators sold as components of nuclear steam supply systems. The contracts require the provision of certain products and services at prices discounted at varying rates together with cash payments. Tolling agreements have been entered into with some parties who have asserted steam generator claims. As at 31 March 2004, tolling agreements existed for two claims. Provisions have been made for the best estimate of costs to settle these matters. The liabilities are expected to be satisfied over the next 10 to 12 years, with the majority of expenditure occurring over the next six years. The provisions are discounted at 3.2%. The provisions are sensitive to a number of factors including timing and amount of discounted products and services offered.

The provision for uranium supply contracts relates to the settlement of various contract suits which arose in the late 1970s. Settlements have been agreed whereby the Westinghouse Business Group provide equipment and fuel supplies, of which five remain open as at 31 March 2004. The supply of equipment is essentially complete and the fuel supplies extend through to 2013. The provisions are discounted at 3.2%.

b. Decommissioning and other contract provisions

Other contract provisions relate to loss making contracts and sundry contractual claims. The majority of the provisions are expected to be utilised over the next 11 years.

c. Restructuring and pension costs

The main elements of restructuring costs are voluntary severance obligations. The amounts provided are based on best estimates of the severance costs of employees who have left or will leave under voluntary severance terms. Accrued pension costs of £55 million (2003: £63 million) are also included. The majority of provisions are expected to be utilised over the next 10 to 15 years.

d. Other provisions

Other provisions within the Group include warranty provisions of £22 million (2003: £26 million) and insurance provisions of £30 million (2003: £31 million). The latter represent best estimates of existing self-insurance liabilities for claims incurred but not reported, calculated in accordance with established insurance industry practice. Other provisions within the company reflect net liabilities of certain subsidiaries where investments have already been provided against.

28. Called up share capital

	2004 £m	2003 £m
Authorised		
43,000,000 ordinary shares of £1 each	43	43
Allotted, called-up and fully-paid		
32,668,244 ordinary shares of £1 each	33	33

Notes to the accounts continued**29. Reserves**

	Group Profit and loss account £m	Company Profit and loss account £m
Balance at 1 April 2003	(2,727)	275
Currency translation differences	(10)	—
Loss for the financial year	(194)	(75)
Balance at 31 March 2004	(2,931)	200

A separate profit and loss account for the company has not been published as allowed under section 230 of the Companies Act 1985.

Currency translation differences represent the exposure on foreign currency net assets held by the Group, arising as a result of movements in exchange rates in the year.

30. Reconciliation of movements in Shareholders' funds

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
Loss for the financial year	(194)	(865)	(75)	(16)
Currency translation differences	(10)	18	—	—
	(204)	(847)	(75)	(16)
Opening Shareholders' funds	(2,694)	(1,847)	(308)	324
Closing Shareholders' funds	(2,898)	(2,694)	(383)	(308)

Cumulative goodwill written off to reserves in respect of acquisitions before 1 April 1998 amounts to £119 million (2003: £119 million). This goodwill had been eliminated as a matter of accounting policy prior to the adoption of FRS 10, which requires goodwill acquired as the result of acquisitions to be capitalised on the balance sheet. This will be charged in the profit and loss account if and when the businesses to which it relates are disposed of.

31. Financial commitments

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
Capital commitments contracted for but not provided	138	159	133	151

The Group's operating leases now relate primarily to head office facilities in the US. The annual commitments are not significant and now amount to approximately £10 million per annum.

32. Pensions and other post-retirement benefits**a. Contributions**

The majority of the employees of the Group are covered by four pension schemes which provide defined benefits to members. The Group's contributions to these pension schemes are as follows:

	2004 £m	2003 £m
The Combined Pension Scheme	—	—
BNFL Group Pension Scheme	5	6
Westinghouse Electric Company Pension Plan	26	19
Electricity Supply Pension Scheme	20	10
	51	35

32. Pensions and other post-retirement benefits continued

b. The Combined Pension Scheme

The Combined Pension Scheme (CPS) was set up as a statutory body with effect from 1 July 1997 as a result of merging the previous UKAEA Principal Non-Industrial Superannuation Scheme (PNISS) and the UKAEA Industrial Superannuation Scheme (ISS) and is managed by the UKAEA. It is a multi-employer scheme which provides defined benefits to its members. In common with other public sector schemes the CPS does not have many of the attributes of normal pension schemes. Any surplus of contributions made in excess of benefits paid out in any year is surrendered to the Consolidated Fund and any liabilities are met from the Consolidated Fund via the annual Parliamentary vote. Government does not maintain a separate fund and the scheme valuation is based on a theoretical calculation as to how a typical UK pension scheme would have invested the historical surplus of contributions over payments. There is no actual fund.

The nature of the scheme, supported as it is by the Government's Consolidated Fund and a theoretical portfolio of assets, has required the Group to consider carefully the most appropriate treatment to meet the requirements of FRS 17 and present a true and fair view. Having taken advice, the Group considers that FRS 17 requires the scheme to be accounted for as defined benefit in nature, despite some of its unique features.

The most recent triennial actuarial valuation of the scheme which has been completed is as at 31 March 2000. The next valuation is currently underway. The 31 March 2000 valuation indicated a market value of the notional investments of £2,436 million with a level of notional funding of 130%. As a result of the notional surplus, the pension scheme managers have indicated that there will be a contribution holiday from 1 April 1998 to 31 March 2023 (the average remaining service life of current members at that time). Thereafter the contribution rate will revert to a regular rate of 13.6%. The entry age method was used with the following long-term assumptions:

	%
Notional investment yield (net of pay increase)	2.0
Notional investment yield (net of price inflation)	3.5
Inflation assumption	3.5

c. The BNFL Group Pension Scheme

The BNFL Group Pension Scheme is a funded scheme. Contributions are paid into investment funds operated by Insight. The subsidiaries contribute to the scheme at rates recommended by the scheme's professionally qualified actuaries; these increased from 12% to 14.5% effective from 1 April 2004. The first triennial valuation of the scheme took place as at 31 March 2001 using the projected unit credit method. The market value of the scheme's assets was £93 million with a 109% level of funding. The underlying assumptions used in the valuation were:

	Past service %	Future service %
Investment return	5.6	6.5
Salary increase	3.8	4.0
Pensions increase	2.3	2.5
Inflation assumption	2.3	2.3

A further actuarial valuation of the scheme's assets (effective 31 March 2004) is currently underway, the results of this exercise will not be available until later this year.

Notes to the accounts continued**32. Pensions and other post-retirement benefits continued****d. Westinghouse Electric Company Pension Plan**

Westinghouse Electric Company employees are provided with certain pension and post-retirement benefits through funded schemes. The post-retirement benefits include medical, dental and life insurance benefits. As part of the acquisition of the Westinghouse Electric Company business, there is an agreement to provide similar benefits, subject to the previous owner retaining pension liability related to accrued benefits in respect of employees and former employees for service prior to the date of completion of the acquisition. Westinghouse Electric Company is therefore only liable for benefits accruing to employees after 22 March 1999.

The most recent actuarial valuation of the scheme took place on 31 December 2002. This indicated a market value of the scheme's assets of £77 million and a 66% level of funding. The unit credit cost method was used with the following underlying assumptions:

	%
Discount rate	7.0
Expected long-term rate of return on assets	8.7
Salary increase	3.5
Inflation assumption	2.6
Pensions increase	1.1

e. The Electricity Supply Pension Scheme

Magnox Electric plc employees are members of the Electricity Supply Pension Scheme (ESPS). The ESPS is a funded scheme which, as at the date of the most recent triennial actuarial valuation (effective 31 March 2001), had assets with a market value of £1,305 million, equating to a level of funding of 113.7%. Subsequent to the last formal valuation the value of the schemes assets has however fallen in line with the decline in worldwide equity markets. In the light of this, following a period of reduced contributions (April 2002 to March 2003), the company has, with effect from 1 April 2003, therefore reverted back to a full contribution rate.

The projected unit method was used to calculate the 31 March 2001 valuation with the following underlying assumptions:

	%
Investment return (pre-retirement)	6.3
Investment return (post-retirement)	5.3
Salary increase	3.3
Pensions increase	2.5
Inflation adjustment	2.3

A further actuarial valuation of the scheme's assets (effective 31 March 2004) is currently underway, the results of this exercise will not be available until later this year.

f. FRS 17 valuations

i. The valuations for each of the schemes have been updated on a basis consistent with FRS 17. The major financial assumptions used are:

	CPS			BNFL Group Pension Scheme			Westinghouse Electric Company			ESPS		
	2004 %	2003 %	2002 %	2004 %	2003 %	2002 %	2004 %	2003 %	2002 %	2004 %	2003 %	2002 %
Rate of increase in salaries	4.9	4.9	5.0	4.3	4.0	4.2	2.6	2.8	2.5	3.9	3.6	3.8
Rate of increase in pensions	3.4	3.4	1.1	2.8	2.5	2.7	1.1	1.2	1.0	3.0	2.7	2.9
Inflation assumption	3.4	3.4	3.5	2.8	2.5	2.7	2.6	2.6	2.7	2.9	2.6	2.8
Discount rate	7.0	7.0	3.5	5.5	5.4	6.0	6.0	6.6	6.9	5.5	5.4	6.0

32. Pensions and other post-retirement benefits continued**f. FRS 17 valuations continued**

ii. The fair value of the assets and liabilities for each of the schemes are as follows:

	CPS		BNFL Group Pension Scheme		Westinghouse Electric Company		ESPS	
	2004 £m	2003 £m	2004 £m	2003 £m	2004 £m	2003 £m	2004 £m	2003 £m
Equities	1,774	1,342	73	56	66	54	822	660
Bonds	313	301	32	24	28	23	268	242
Property	—	—	—	—	—	—	96	91
Other	—	—	1	—	—	—	22	4
Total market value of assets	2,087	1,643	106	80	94	77	1,208	997
Present value of scheme liabilities	(1,684)	(1,554)	(141)	(120)	(197)	(166)	(1,339)	(1,249)
Net surplus/(deficit)	403	89	(35)	(40)	(103)	(89)	(131)	(252)
Restriction on surplus	(403)	(89)	—	—	—	—	—	—
Net pension liability	—	—	(35)	(40)	(103)	(89)	(131)	(252)

In the case of the CPS, the assets and any surplus or deficit are notional only. Due to the notional nature of the assets supporting the scheme and the fact that the Group has no rights to the surplus other than as allowed by the scheme managers, the Group does not consider that on full implementation of FRS 17 it would be prudent or appropriate to recognise any surplus on the balance sheet. The surplus of £403 million as disclosed above for the CPS has therefore been restricted in accordance with the requirements of FRS 17.

iii. The expected rates of return for each of the schemes are:

	CPS			BNFL Group Pension Scheme			Westinghouse Electric Company			ESPS		
	2004 %	2003 %	2002 %	2004 %	2003 %	2002 %	2004 %	2003 %	2002 %	2004 %	2003 %	2002 %
Equities	7.0	7.0	7.0	7.0	7.0	7.5	8.5	8.8	12.1	7.7	7.6	7.7
Bonds	4.5	4.5	2.5	4.7	4.5	5.0	6.7	7.3	7.1	4.8	4.8	5.7
Property	—	—	—	—	—	—	—	—	—	6.7	6.6	6.2
Other	—	—	—	4.7	4.5	5.0	—	—	2.3	4.3	3.8	3.7

iv. The movements in the surplus/(deficit) in the year are as follows:

	CPS £m	BNFL Group Pension Scheme £m	Westinghouse Electric Company £m	ESPS £m	Total excluding CPS £m
Surplus/(deficit) in scheme at 1 April 2003	89	(40)	(89)	(252)	(381)
Current service cost	(59)	(6)	(19)	(18)	(43)
Contributions	17	5	26	20	51
Past service cost	—	(1)	—	(7)	(8)
Expected return on pension scheme assets	110	5	7	—	12
Interest on pension scheme liabilities	(100)	(6)	(12)	—	(18)
Actuarial gains/(losses):					
Actual return less expected return on pension scheme assets	346	13	(1)	174	186
Experience gains and losses arising on the scheme liabilities	—	—	—	(7)	(7)
Changes in assumptions underlying the present value of the scheme liabilities	—	(5)	(15)	(41)	(61)
Surplus/(deficit) in scheme at 31 March 2004	403	(35)	(103)	(131)	(269)

Notes to the accounts continued

32. Pensions and other post-retirement benefits continued**g. Impact on the Group's primary statements**

If the assets and liabilities of the BNFL Group Scheme, the Magnox Electric Group part of the ESPS and the Westinghouse Electric Company Pension plan had been recognised in the Group's financial statements, the Group would have additional net liabilities of £269 million (2003: £381 million reduction in net liabilities). The impact on the consolidated profit and loss account would have been:

	2004 £m	2003 £m
Analysis of the amount that would have been charged to operating profit		
Current service cost	43	40
Past service cost	8	11
Total operating charge	51	51
Analysis of amount that would have been credited/(charged) to other finance income		
Expected return on pension scheme assets	12	33
Interest on pension scheme liabilities	(18)	(13)
Net (expense)/return	(6)	20

The impact on the consolidated statement of total recognised gains and losses (STRGL) would have been:

	2004 £m	2003 £m
Analysis of amount that would have been recognised in STRGL		
Actual return less expected return on pension scheme assets	186	(346)
Experience gains and losses arising on the scheme liabilities	(7)	47
Changes in assumptions underlying the present value of the scheme liabilities	(61)	(91)
Actuarial gain/(loss) that would have been recognised in STRGL	118	(390)

h. History of experience gains and losses

	2004	2003
Actual return less expected return on pension scheme assets (£ million)	186	(346)
Percentage of scheme assets	5%	(12)%
Experience gains and losses arising on the scheme liabilities (£ million)	(7)	47
Percentage of the present value of scheme liabilities	–%	2%
Total amount recognised in STRGL (£ million)	118	(390)
Percentage of the present value of scheme liabilities	4%	(13)%

33. Contingent liabilities

a. At 31 March 2004, the company had contingent liabilities incurred in the ordinary course of business arising out of guarantees and other transactions in respect of which, in the opinion of the directors, no material losses are expected to arise:

i. Guarantees, indemnities and charges have been given to banks, insurance companies and other organisations in respect of credit and foreign exchange facilities of £387 million (2003: £517 million) relating to overseas subsidiaries and £16 million relating to subsidiaries located in the UK.

ii. Letters of support have been provided to certain subsidiaries, in particular Magnox Electric plc, in order for them to continue operating safely and to meet their liabilities as they fall due for the foreseeable future. The net liabilities of Magnox Electric plc, as disclosed in its accounts, amount to approximately £3.7 billion (2003: £3.5 billion).

33. Contingent liabilities continued

iii. The Group and its subsidiaries have entered into various guarantees in respect of contract performance, working capital facilities, technical services and plant maintenance, in the ordinary course of business.

iv. £91 million (2003: £81 million) of funds within current asset investments and short-term deposits (within note 17) are held within charge over deposit accounts (CODAs). These represent funds provided by customers which are held in accounts controlled and owned by the company, but over which the customer has a legal charge until the associated work has been completed.

v. Bank pooling guarantees in respect of the company and certain UK subsidiaries.

b. On 21 March 1994, four residents of Dundalk, Ireland commenced proceedings in the High Court of Dublin against Ireland and the Attorney General and BNFL. The first part of the plaintiffs' claim relates to regulatory matters, specifically to allegations that EC Directives have not been fully complied with in the UK. Following a trial of this part of the claim the Irish Court decided that it did not have jurisdiction to determine these issues or grant the remedies requested by the plaintiffs. Subject to a possible appeal by the plaintiffs, this judgment, in effect, brings to an end this element of the claim. The second part is a tort claim in which damages are sought for alleged assault, nuisance, trespass, wrongful acts and unlawful interference with the plaintiffs' constitutional right of bodily integrity, which it is claimed have arisen as a result of discharges from Sellafield. This aspect of the claim remains in its early stages and no orders have been made as to the future management of the case. It is therefore difficult to assess the financial consequences of the case though BNFL remains committed to vigorously defending the allegations, which it believes have no merit.

c. As described in note 24, fundamental uncertainties remain regarding the measurement of nuclear liabilities and the timing of the cash flow. Until the new structure announced by Government is established and responsibility for these liabilities transferred, the impact of any additional liabilities could materially affect the results of operations and financial condition of the Group.

34. Related party transactions and controlling party

The following table summarises the disclosures required by FRS 8 regarding related parties:

	Undertakings under common control £m	Joint ventures £m	Associated undertakings £m
2004			
Turnover	243	6	5
Purchases	12	8	3
Trading amounts due from related parties at 31 March	82	1	—
2003			
Turnover	223	3	6
Purchases	5	12	4
Trading amounts due from related parties at 31 March	71	—	—

The ultimate controlling party of the company is considered by the directors to be Her Majesty's Government. Undertakings under common control of the Government are the Ministry of Defence (MoD) and the UK Atomic Energy Authority. For further details regarding equity and loan transactions with associated undertakings and joint ventures refer to note 12.

In addition to the trading balances disclosed above, £162 million (2003: £216 million) is owed to the Group by the MoD. This represents reimbursement by the MoD of advances made by the Group to United Kingdom Nirex Limited in respect of the disposal cost of waste arising on BNFL sites to 31 March 2001. £55 million (2003: £nil) is included within other debtors falling due within one year and £109 million (2003: £216 million) is included within other debtors falling due after more than one year.

Notes to the accounts continued

35. Derivatives and other financial instruments

As explained on page 63 note 1(o) the Group uses derivatives and other financial instruments in managing the risk associated with its business. With the exception of commodity contracts in respect of electricity trading (dealt with in note 35d below), the Group does not engage in speculative treasury arrangements, and all of its activities are designed to support underlying business activities. All treasury activities are carried out under policies approved by the Board. The following numerical analysis gives an indication of the significance of these instruments to the Group.

a. Fair value of derivatives and other financial instruments

Set out below is a comparison of the book values and fair values of the Group's derivatives and other financial instruments (excluding short-term debtors and creditors). Fair values have been based on published market prices (for listed instruments) or estimates made from discounted cash flow analysis (for unlisted instruments). The fair value of the net financial assets and derivatives is £257 million (2003: £258 million) in excess of book value. Certain other assets and liabilities held by the Group, most notably the Secretary of State's Undertaking, have not been assigned a fair value as the instruments are not readily traded or because their book value approximates to their fair value.

	Book values		Fair values	
	2004 £m	2003 £m	2004 £m	2003 £m
Financial assets				
Nuclear Liabilities Investment Portfolio (note 12f)	4,016	3,843	4,253	4,078
Gilt investments (note 17)	228	235	244	258
Managed investments (note 17)	608	548	608	548
Short-term deposits (note 17)	686	1,039	686	1,039
Loans and advances to associated undertakings and joint ventures (notes 12 and 14)	10	10	10	10
Debtors falling due after more than one year	132	241	132	241
Trade investments (note 12e)	3	3	3	3
Cash	128	72	128	72
	5,811	5,991	6,064	6,249
Financial liabilities				
Overdraft (note 18)	(9)	(3)	(9)	(3)
Loans (note 20)	(27)	(51)	(27)	(51)
Obligations under finance leases (note 18)	(2)	(3)	(2)	(3)
Other creditors falling due after more than one year (note 19)	(12)	(17)	(12)	(17)
	(50)	(74)	(50)	(74)
Derivatives				
Foreign currency contracts (see 35b(ii) below)	15	—	19	—
Net financial assets and derivatives	5,776	5,917	6,033	6,175

b. i. Currency exposure

Set out below is an analysis of the Group's exposure to financial instruments denominated in currencies other than the operational currency of the individual business units. These currency exposures are disclosed after taking into account derivatives and other financial instruments entered into to manage the Group's exchange rate positions.

Functional currency of operation	Net foreign currency monetary assets/(liabilities)			
	US Dollar £m	Euro £m	Other £m	Total £m
Sterling	11	1	19	31
At 31 March 2004	11	1	19	31
Sterling	37	(4)	21	54
US Dollar	—	—	14	14
At 31 March 2003	37	(4)	35	68

35. Derivatives and other financial instruments continued**b. ii. Hedges**

Board policy is that all significant firm foreign exchange transaction exposures should be hedged. This is done by forward contracts, currency options or, where appropriate, by matching receipts and payments in the same currency. Where their guidelines permit, the investment managers of the Captive Insurance Subsidiaries may invest in non-sterling instruments; this is controlled by limiting the amount of such investments which may be left unhedged to a percentage of the total portfolio. At 31 March 2004 the Captives held no significant unhedged exposures.

The fair value of derivatives of £19 million (2003: Enil) as disclosed in note 35a relates to the following:

	2004		2003	
	Gains £m	Losses £m	Gains £m	Losses £m
Recognised as at 31 March	15	—	—	—
Unrecognised as at 31 March	16	(12)	16	(16)
	31	(12)	16	(16)

Recognised gains in the table above relate to currency options. The unrecognised gains/(losses) are expected to be recognised as follows:

	2004		2003	
	Gains £m	Losses £m	Gains £m	Losses £m
Within one year	7	(7)	11	(11)
After more than one year	9	(5)	5	(5)
	16	(12)	16	(16)

c. Interest rate risk

The tables below summarise the interest rate profile of the Group's financial instruments (excluding short-term debtors and creditors) after taking into account the effect of any interest rate or currency derivatives used to manage the risk associated with these instruments. Financial assets and liabilities are as analysed in note 35a.

i. Financial assets

	Floating rate £m	Fixed rate £m	Non interest bearing £m	Total £m	Fixed rate instruments	
					Weighted average interest rate %	Weighted average period to maturity Years
Sterling	3,578	1,577	473	5,628	4.1	2.3
US Dollar	141	—	—	141	—	—
Euro	26	—	9	35	—	—
Other	7	—	—	7	—	—
Total financial assets at 31 March 2004	3,752	1,577	482	5,811	4.1	2.3
Sterling	4,491	886	503	5,880	4.5	2.7
US Dollar	101	—	—	101	—	—
Euro	6	—	—	6	—	—
Other	4	—	—	4	—	—
Total financial assets at 31 March 2003	4,602	886	503	5,991	4.5	2.7

Notes to the accounts continued

35. Derivatives and other financial instruments continued

c. Interest rate risk continued

i. Financial assets continued

Financial assets bearing no interest can be analysed as follows:

	2004 £m	2003 £m
Funds within Nuclear Liabilities Investment Portfolio	21	21
Investments and short-term deposits: equity investments in Captive Insurance Subsidiaries	321	228
Debtors falling due after more than one year	127	241
Advances to associated undertakings and joint ventures	10	10
Trade investments	3	3
	482	503

Debtors due in more than one year have a weighted average period to maturity of 1.1 years (2003: 1.5 years).

ii. Financial liabilities

	Floating rate £m	Fixed rate £m	Non interest bearing £m	Total £m	Fixed rate instruments Weighted average interest rate %	Weighted average period to maturity Years
Sterling	2	—	10	12	—	—
US Dollar	30	2	—	32	7.7	2.0
Euro	6	—	—	6	—	—
Total financial liabilities at 31 March 2004	38	2	10	50	7.7	3.0
Sterling	4	—	16	20	—	—
US Dollar	52	2	—	54	7.7	3.0
Total financial liabilities at 31 March 2003	56	2	16	74	7.7	3.0

Included within financial liabilities bearing no interest are other creditors due after one year of £10 million (2003: £16 million), which have a weighted average period to maturity of 3.0 years (2003: 7.1 years).

Floating rate assets and liabilities, which include bank loans and deposits, borrowings and index-linked bonds, have interest rates which vary in accordance with market rates over periods ranging from three days to a year. Coupons on the index-linked gilts are reset every six months in line with inflation. The interest rate characteristics of the Secretary of State's Undertaking are explained in note 16.

d. Commodity contracts

Under the electricity trading arrangements effective from 27 March 2001, a small number of low value contracts are entered into, in order to take trading positions in the market. The fair value of these instruments at 31 March 2004 is negligible (2003: £nil). The estimate is based on a comparison between the contracted price (specified at the date of the deal) and the price for a similar contract at the year end (based on available market data). All of these instruments will expire in the course of the next financial year.

e. British Energy contracts

During the year, a revised contract was agreed with British Energy for the supply of nuclear fuel. This contract includes an element that is dependent on the market price of electricity. Part of the price which the Group receives for supplying fuel under this contract decreases with each £1/Mwh drop in market price of electricity below £18/Mwh with a floor at £15/Mwh. The Group's maximum annual exposure under this arrangement is £15 million. This element of the contract is effectively a financial derivative. At the year end however, based on forecasts of electricity prices, the estimated fair value of the derivative is £nil.

As a result of entering into this contract, the Group now shares part of the risk of fluctuating electricity prices with its customer. The Board has considered this risk but, based on its view of medium-term electricity prices, has concluded that the costs of hedging the risk of exposure would outweigh the potential benefits.

Background to nuclear liabilities

The safe treatment and disposal of waste and ultimate decommissioning of our facilities are fundamental responsibilities of the Group. These activities will take place over long timescales unique to the nuclear industry. The financial liabilities that arise from these activities have to take account of numerous uncertainties including the nature of the waste, its final destination and the ultimate status of our sites. It is these very uncertainties over such long timescales which make Government plans to restructure, fund and manage the liabilities through the NDA so important.

Background

The Group's nuclear liabilities arise from the operation of facilities for the production of nuclear fuel, the generation of electricity using first generation Magnox nuclear reactors, reprocessing of fuel to separate reusable nuclear materials from the small amount of waste product and, most significantly, managing the legacy of historical nuclear industry activity. The major part of this latter activity is carried out at Sellafield. A significant amount of the company's plant and equipment used in this process was already in existence when BNFL was formed in 1971 to take over the assets of and activities previously carried out by the UK Atomic Energy Authority (UKAEA). Those activities stemmed from a military programme during the Cold War, and the priority when the plants were built was to make them operational and effective as quickly as possible. When these plants were designed, limited thought was given to treating and disposing of the waste produced and their ultimate decommissioning and demolition. As a result the costs of so doing are now very considerable.

The challenge of estimating future costs

The task of assessing how best to decommission the Group reactors, how waste can be retrieved from the original storage facilities, and then treated for long-term storage/disposal, or how decommissioning and dismantling of these early plants should be carried out, is itself very difficult. For example, records of plant design and operations leave a number of unanswered questions, including the exact quantities and chemical composition of historic wastes. The long period over which these wastes have been stored, in some cases under water, has resulted in deterioration in the condition of the wastes and the storage facilities. Consequently, characterisation of the wastes, and design of technical solutions required to retrieve the wastes to enable treatment, will be difficult and demanding and will require innovative treatment solutions. New waste treatment plants that may be required to handle these wastes must be physically integrated into Sellafield's already complex infrastructure, and the construction of plants on such a site itself presents unique engineering challenges. Although the

Group has considerable experience of delivering high quality safe solutions to such complex problems, considerable uncertainties remain, and will do so until work is done over a number of years to study further the historic wastes stored and the condition of the buildings. For plants designed and built later, waste treatment, decommissioning and dismantling issues were considered during the design and operation stage, and the relative costs are therefore lower, estimating these costs is therefore easier, and assumptions can be made with greater confidence.

Inherent uncertainty

The company has made its estimates for many years by making assumptions about the likely safety and environmental requirements based on the best information available today. The process takes into account known and foreseeable developments in technology. This is then used as the basis for estimating the costs, which itself involves making judgements, not only about the likely duration of the individual tasks, the equipment required and the implications for costs, but also the likely range of possible variations around the judgements selected as the base, or working assumption. Once this has been estimated, a further allowance is calculated for possible but less likely outcomes or circumstances and for trends in labour costs. Estimates of cost, expressed in terms of today's money are then discounted to take into account the fact that the tasks will not be carried out for a long time, as described further below. Whilst the estimation process is carried out as thoroughly as possible, the inherent uncertainties arising from the nature and age of the facilities mean that there can be no firm guarantee that the resulting provisions may not prove too large, nor on the other hand that they will necessarily prove adequate. As highlighted in note 24 to the accounts, in the particular area of historic wastes relating to the military and early civil nuclear programmes, work undertaken to revisit the waste retrieval and disposal strategy highlighted significant uncertainty as to the quantities and composition of these wastes. The Board has used the best available knowledge to estimate the related liabilities but, pending several more years' work, it is not possible to quantify the financial implications of a range of possible alternative outcomes or circumstances with the degree of certainty required to enable an estimate of this risk to be recorded in the balance sheet. The accounts, therefore, disclose this specific uncertainty which could result in a significant and material impact on the Group's results and financial position at the point at which it crystallises. As additional knowledge of the nature and quantity of waste becomes available the estimate will be refined. Another key area of uncertainty as outlined in note 4, relates to the Group's reactor decommissioning liabilities.

Background to nuclear liabilities

Timescales for decommissioning

Natural decay in radioactivity means that by delaying some decommissioning tasks, the radiation exposures to people engaged in dismantling plants reduces dramatically. For example, deferring final decommissioning until 135 years after a nuclear reactor shuts down would see radiation levels inside the reactor decrease to one millionth of their original levels. However, delay cannot be indefinite, because the physical structures of buildings ultimately deteriorate, even when these buildings are kept in a safe state by an ongoing process of routine maintenance. Therefore, for both safety, hazard reduction and cost reasons, decommissioning plans aim to achieve the best balance between deferring dismantling tasks to allow radioactivity to reduce, whilst ensuring that the expected state of buildings and structures is not itself the cause of increased risk and complexity.

The timescale ultimately assumed also has a profound effect on the estimate of the accounting provisions required today for future decommissioning and waste management costs. Changes in the assumed timescale could increase or reduce such costs significantly.

Destination of nuclear waste

Significant quantities of slightly or partially radioactive material will result from decommissioning and dismantling plant, equipment, buildings and infrastructure. By far the largest volume of these materials is expected to be categorised as low-level waste, the same category into which radioactive wastes arising from medical use usually fall. However, some materials are expected to be classified as intermediate-level waste and some small quantities, mainly arising from reprocessing and waste management, as high-level waste. The previous assumption of both Government and of the nuclear industry has been that intermediate- and high-level wastes would be placed underground, whether permanently or in retrievable form, in facilities specially created for this purpose. Whilst this is now subject to public consultation, the question of where these wastes will be deposited is one of critical importance to the estimation of the future costs of waste disposal.

Low-level wastes are presently disposed in a permanent facility at Drigg near to the Sellafield plant. This has been used for many years for all national low-level wastes. As the only route for the disposal of this low-level waste, Drigg is a national asset. In recent years, increasingly costly techniques have been used to compact waste for disposal at the site so as to maximise the remaining capacity and delay for as long as possible the point at which the existing site becomes full.

Intermediate- and high-level waste are planned to be sent for underground storage, in separate repositories, which is significantly more costly than above ground storage. Furthermore, the estimation of costs is inherently difficult because it is dependent both on an estimate of the likely cost of facilities (which itself is much affected by the geological circumstance of the chosen location) and by the likely volume of wastes from all sources that would be placed there. Nirex, based at Harwell in Oxfordshire, was set up in the early 1980s in agreement with the UK Government to examine the options for disposing radioactive waste in a deep underground repository. Its Shareholders are BNFL (74.5%), British Energy (10.8%) and the UKAEA (14.7%). Previously, we had based our calculations of waste disposal costs on updating estimates produced by Nirex some years ago for the costs of using an underground facility. With the passage of time, and the continuing absence of any proposed location for an underground disposal site, the Board of BNFL has reassessed the reasonableness of continuing with the assumption that such a disposal facility will be built in the short- or medium-term future. Whilst the national strategy for ultimate waste disposal is reviewed, it is the Board's view that underground disposal will not in fact be available in the short- to medium-term. As a result, we continue to make provision for maintaining safe and secure storage facilities for at least 100 years by which time it is assumed that a repository will be available and disposal will be underway.

Uranium and plutonium

The Group owns quantities of plutonium and treated uranium. Plutonium is of considerable value for civil purposes if used in fast breeder reactors and MOX fuel. Uranium has value in a continuing nuclear programme as it is the essential starting element in creating nuclear fuel. The Group's stocks of treated uranium and plutonium are regarded as assets, but all costs incurred in creating these have always been written off as incurred. As a result, these materials, which in some cases may require extensive treatment prior to reuse, are carried at nil value. Some of these stocks remain the property of customers, and all are subject to international non-proliferation agreements and to oversight by the international body responsible for the control of nuclear materials. There is no agreed process for disposing of plutonium if either the material is not required or treatment for reuse proves uneconomic, and pending reuse, therefore, the Group does not provide for disposal costs. All stocks are stored in secure conditions and, subject to demand for MOX fuel, are likely to remain so for a long time.

The ultimate status of sites

The Board of BNFL has long estimated its provisions for decommissioning and waste management on the assumption that the existing plants and buildings are demolished and sites are cleared, but not to the extent that the sites would be returned to farmland. This reflects the approach which industry typically follows where there is no requirement in law or otherwise to do more than ensure that an industrial site is made safe. In the case of the historic waste storage facilities, the extent of decommissioning during the next century will be defined by considering the requirements to render the wastes that these contain safe for long-term storage, the need to reduce radioactive discharges and the protection of our workforce from unnecessary exposure to radiation. Removing all of the historic wastes would increase the length of the retrievals operations by many years which would in turn require waste treatment plants to be kept open and delay decommissioning of the Sellafield site. For certain plants, therefore, it would be illogical to visualise removing the whole of a building including its foundations from the site – excavating the foundations and relocating the waste to another site is unlikely to be justified on cost, environmental or safety grounds.

Discounting

The Group's provisions for nuclear liabilities are discounted to reflect the incidence of anticipated expenditures and the long delay before many of these expenditures are expected to occur.

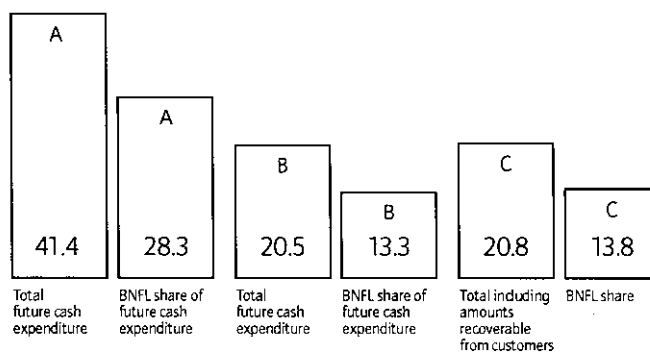
This follows required accounting practice. A discount rate of 2.5% is applied, reflecting an estimate of a long-term rate of investment return after accounting for risk and taxation. The Group's investments and the terms of the financial undertaking from the Secretary of State in respect of certain nuclear liabilities related to the Magnox fuel cycle are expected to generate such a return. Each year, as we become one year closer to discharging our liabilities, our provisions are increased by 2.5% to reflect the removal of one year's discounting. This, together with the impact of changes in price level, is known as revalorisation. The charge is recognised as part of the Group's interest expense with interest earned on the investments and Secretary of State's undertaking reflected as interest receivable.

Nuclear liabilities

The Group's nuclear liabilities can be analysed as illustrated in the chart below.

The Group's share of discounted future cash expenditure and the amount provided on the Group's balance sheet are different due to the fact that a proportion of the liability has not yet been recognised as it will be reflected in the accounts in line with future operations. An element of non-cash costs exists in the provisions balance and relates to the remaining depreciation on capital assets already acquired and paid for, which will be charged against provisions over the remaining useful life of those assets.

GROUP NUCLEAR LIABILITIES
31 MARCH 2004 £ BILLION



A UNDISCOUNTED
B DISCOUNTED
C BALANCE SHEET PROVISION

Principal subsidiary and associated undertakings and joint ventures

Subsidiary and associated undertakings and joint ventures whose results did not, in the opinion of the directors, materially affect the profit or the assets of the Group are not shown. Unless otherwise stated, subsidiaries are incorporated in the United Kingdom.

Subsidiary undertakings

Magnox Electric plc

It is wholly owned by BNFL and its purpose is to generate and supply electricity.

Westinghouse Electric Company LLC

Incorporated in the United States of America, it is wholly owned by BNFL Nuclear Services Inc. (BNSI) which in turn is wholly owned by BNFL USA Group Inc. Its purpose is to pursue business opportunities related to the commercial nuclear power industry. Its headquarters is The Energy Centre, Monroeville, Pennsylvania.

BNFL Inc.

Incorporated in the United States of America, it is wholly owned by BNFL USA Group Inc. and its purpose is to identify and pursue business opportunities in North America.

British Nuclear Group Limited

It is wholly owned by BNFL and its purpose is to act as a holding company.

International Nuclear Fuels Limited (INFL)

It is wholly owned by BNFL and its purpose is to develop international business through collaboration.

INFL has a 62.5% shareholding in Pacific Nuclear Transport Limited, whose main purpose is the transport of spent fuel and associated services.

BNFL Uranium Asset Management Company Limited

It is wholly owned by BNFL and its purpose is to provide uranium contract management services.

Direct Rail Services Limited

It is wholly owned by BNFL and its purpose is to provide nuclear rail transport services within the UK.

Deva Manufacturing Services Limited

It is wholly owned by BNFL and its purpose is to manufacture waste drums and associated equipment.

Fellside Heat and Power Limited

It is wholly owned by BNFL and its purpose is to produce electricity through combined heat and power.

Hinton Insurance Limited

Incorporated in Guernsey, it is wholly owned by BNFL and its purpose is to act as an insurer.

Rutherford Indemnity Limited

Incorporated in Guernsey, it is wholly owned by BNFL and its purpose is to act as an insurer.

Electricity Producers Insurance Company Limited

Incorporated in Guernsey, it is wholly owned by BNFL and its purpose is to act as an insurer.

Electricity Producers Insurance Company (Bermuda) Limited

Incorporated in Bermuda, it is wholly owned by BNFL and its purpose is to act as an insurer.

BNFL Investments US Limited

It is wholly owned by BNFL and its purpose is to act as a holding company for BNFL's interests in the US.

BNFL Properties Limited

It is wholly owned by BNFL and its purpose is to purchase and lease UK commercial property.

BNFL Enrichment Limited

It is wholly owned by BNFL and is the holding company for the Group's interest in Urenco Limited.

Associated undertakings

Urenco Limited

Its main purpose is the supply of enriched uranium produced in enrichment plants using the centrifuge process. BNFL Enrichment Limited holds one-third of the shares. The remainder are held by Dutch and German organisations.

Enrichment Technology Company Limited

Its purpose is to provide centrifuges and centrifuge technology for uranium enrichment including plant design and research and development. The effective holding by BNFL is one third of the shares through both BNFL Enrichment Limited and Urenco Limited. The remainder are held by Dutch and German organisations.

Joint ventures

Westinghouse Government Environmental Services Company LLC

Its purpose is to pursue non defence related US Government and environmental business. Its headquarters is The Energy Centre, Monroeville, Pennsylvania.

BNSI holds a 40% membership interest. The remaining membership interest is held by Washington Group International Inc. BNSI has the right to nominate two directors and the concurrence of these directors is required for a number of strategic policy decisions.

Westinghouse Government Services Company LLC

Its purpose is to pursue business opportunities related to the defence programme of the US Department of Energy and the US Department of Defense. Its headquarters is The Energy Centre, Monroeville, Pennsylvania.

BNSI does not hold any legal membership interest but has been assigned a 40% economic interest by Washington Group International Inc. BNSI has the right to nominate one director and the concurrence of this director is required for a number of strategic policy decisions.

United Kingdom Nirex Limited

Its purpose is to provide disposal services for low and intermediate-level waste.

BNFL holds 39.5% of the ordinary shares and Magnox Electric plc holds 35%. The remainder are held by other United Kingdom organisations. The Group does not exercise control as strategy decisions are subject to unanimous Shareholders' approval.

AWE Management Limited

Its purpose is to manage and facilitate the Aldermaston weapons facilities on behalf of the Ministry of Defence. BNFL holds 33% of the ordinary shares. The remainder are held by Lockheed-Martin and Serco.

Financial statistics

	2004	2003	2002	2001	2000	1999 Restated
	£m	£m	£m	£m	£m	£m
Results						
Group turnover	2,322	2,219	2,261	2,146	2,064	1,565
(Loss)/profit before investment income, interest and taxation	(279)	(954)	(2,378)	(103)	(359)	125
Net financing (charges)/income	(20)	(134)	50	37	22	93
(Loss)/profit on ordinary activities before taxation	(299)	(1,088)	(2,328)	(66)	(337)	218
(Loss)/profit for the financial year	(194)	(865)	(2,090)	(46)	(262)	132
(Loss)/profit transferred to reserves	(194)	(865)	(2,090)	(46)	(262)	67
Assets employed						
Fixed assets	11,969	12,233	12,662	12,168	11,407	10,713
Net current assets	11,975	11,112	11,088	10,629	10,687	10,065
Creditors: amounts falling due after more than one year	(4,895)	(4,000)	(4,430)	(4,575)	(4,244)	(3,947)
Provisions for liabilities and charges	(21,944)	(22,035)	(21,163)	(17,969)	(17,538)	(16,253)
Net (liabilities)/assets	(2,895)	(2,690)	(1,843)	253	312	578
Financed by						
Share capital	33	33	33	33	33	33
Profit and loss account	(2,931)	(2,727)	(1,880)	218	277	543
Shareholders' funds	(2,898)	(2,694)	(1,847)	251	310	576
Minority interests	3	4	4	2	2	2
	(2,895)	(2,690)	(1,843)	253	312	578

The figures stated above have been taken from the published accounts for each year with the exception of the 1999 figures which have been restated for the effects of accounting policy changes. These restatements were made during 2000 as a result of the adoption of revised accounting policies and the publication of new accounting standards.

Glossary

AGR Advanced Gas-cooled Reactor. A design of nuclear reactor owned and operated by British Energy in the UK.

AMWTP Advanced Mixed Waste Treatment Project.

AP1000 New generation of Advanced Pressurised Water Reactors (PWR) designed by Westinghouse.

AWE Atomic Weapons Establishment.

BWR Boiling Water Reactor.

CO₂ Carbon dioxide, the main greenhouse gas emitted into the atmosphere.

COMARE Committee on Medical Aspects of Radiation in the Environment.

DRS Direct Rail Services (a BNFL subsidiary company).

ETTP East Tennessee Technology Park.

Greenhouse gases Various gases which when released into the atmosphere increase the greenhouse effect, causing climate change.

IERS International Environmental Rating System.

IRIS International Reactor Innovative Secure project.

LMU Liabilities Management Unit.

Magnox A type of reactor, so called because of the magnesium alloy cladding used to contain uranium fuel rods.

MOX Mixed oxide fuel – fuel containing both plutonium and uranium in the form of a ceramic.

mSv A millisievert is one thousandth of one sievert. For example, the average annual amount received from natural background radiation is 2.2 mSv.

NDA Nuclear Decommissioning Authority.

NII Nuclear Installations Inspectorate – part of the Health and Safety Executive, responsible for nuclear safety in the UK.

NLIP Nuclear Liabilities Investment Portfolio.

NRC Nuclear Regulatory Commission (USA).

OSHA Occupational Safety and Health Administration. Part of the US Department of Labor – responsible for health and safety at work.

OXERA Oxford Economic Research Associates.

Oxide fuel Fuel used in Pressurised Water Reactors.

PBMR Pebble Bed Modular Reactor. A new type of reactor currently being developed by a group of companies led by the South African utility company Eskom and involving BNFL.

PWR Pressurised Water Reactor – common type of nuclear reactor used throughout the world.

Remediation To return a site to an appropriate environmental standard.

RoSPA Royal Society for the Prevention of Accidents.

SM&OS Sellafield Management and Operations Services, a business within the former Government Service Group. Now part of British Nuclear Group.

SMP Sellafield MOX Plant – plant designed to make MOX fuel.

tes tonne, a weight equivalent to 1,000kg.

Thorp Thermal Oxide Reprocessing Plant. Reprocesses AGR, PWR and BWR fuel at Sellafield.

TRIR Total Recordable Incidence Rate.

TWh Terawatt-hour – one terawatt-hour represents one hour of electricity consumption at a constant rate of one terawatt. One terawatt equals one million megawatts.

UKAEA United Kingdom Atomic Energy Authority.

URA University Research Alliance.