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XRO Limited

Directors' Report and Financial Statements for the year ended 31 December 2002



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XEROX®

XRO Limited

Directors' Report and Financial Statements for the year ended 31 December 2002

Directors as at 31 December 2002

M.J. Barrett
N.A Blanche
N.S. Mackintosh
J.F.Lawler

Company Secretary

M.J. Barrett

Registered Office

6 Connaught Place
London
W2 2EZ

Registered Auditors

PricewaterhouseCoopers LLP, Uxbridge

Registered Number

324504

XRO LIMITED
DIRECTORS' REPORT
FOR THE YEAR ENDED 31st DECEMBER 2002

The Directors present their report together with the audited financial statements of XRO Limited ("XRO" or the "Company") for the year ended 31 December 2002.

1. PRINCIPAL ACTIVITIES, BUSINESS REVIEW AND FUTURE DEVELOPMENTS

XRO Limited acts as an intermediate holding company for Xerox Corporation's interests in Europe and parts of Africa and Asia. The level of business and the year-end financial position were consistent with expectations. The Directors expect that the current activities will continue for the foreseeable future.

2. RESULTS AND DIVIDENDS

The results for the financial year was £nil. No dividends were proposed and paid during the financial year (note 2.B). No final dividend is proposed. Retained result for the year was £ nil.

3. DIRECTORS

The Directors of the Company at 31 December 2002 who served throughout the year are listed on page 2. Mr. J.F.Lawler resigned as a director on 28th January 2003. Mr. N.A.Blanche was appointed as a director on 23rd of September 2002.

4. DIRECTORS' INTERESTS IN SHARES OF THE COMPANY

No Director had any interests in the shares of the Company at any time during the year.

5. XEROX CORPORATION

In June 2002, Xerox Corporation, the ultimate parent company, announced a new Credit Facility of \$4.2bn, replacing the \$7bn Revolving Credit Facility of 1997. At this time, Xerox Corporation repaid \$2.8bn of the old Revolver and extended the maturity of the remaining \$4.2bn, which predominantly matures in 2005.

Xerox Corporation manages its financing arrangements on a global basis; accordingly, XRO's funding requirements are dependent on the above agreement.

On 11 April 2002, Xerox Corporation reached a settlement with the Securities and Exchange Commission (SEC), relating to matters which had been under investigation by the SEC. Xerox Corporation restated its accounts for the periods from 1997 to 2001. That restatement does not affect the financial statements of XRO.

Significant Xerox Corporation 2003 event

Recapitalisation

In June 2003, Xerox Corporation announced a \$3.6billion recapitalisation that included public offerings of common stock, 3-year mandatory convertible preferred stock and 7 year and 10 year senior unsecured notes as well as a new \$1billion credit facility.

The new facility consists of a \$700million revolving facility and a \$300million term loan both maturing in September 2008. The sale of common stock and mandatory convertible preferred stock raised \$1.4billion. The recapitalisation also included the sale of \$1.2billion senior unsecured notes.

Xerox used net proceeds from the public offerings and new credit facility as well as a portion of its current cash balance to prepay and terminate, with immediate effect, the existing bank credit facility.

6. AUDITORS

Following the conversion of our auditors PricewaterhouseCoopers to a Limited Liability Partnership (LLP) from 1 January 2003, PricewaterhouseCoopers resigned on 27th February 2003 and the directors appointed its successor, PricewaterhouseCoopers LLP, as auditors. A resolution to reappoint PricewaterhouseCoopers LLP as auditors to the company will be proposed at the annual general meeting.

7. DIRECTORS' RESPONSIBILITIES

The Directors' responsibilities are set out on page 14.

By order of the Board of the 23 July 2003



M.J. Barrett,
Company Secretary

XRO LIMITED
PROFIT & LOSS ACCOUNT
FOR THE YEAR ENDED 31 DECEMBER 2002

	<i>Note</i>	2002 £m	2001 £m
Operating profit/(loss)		-	-
Dividend income from group companies		-	450
Profit on ordinary activities before tax		-	450
Tax on profit on ordinary activities		-	-
Profit for the financial year	2A	-	450
Dividends proposed and paid (Including Non-Equity)	2B	-	(450)
Retained results for the financial year		-	-

The notes on pages 8 to 13 form part of these financial statements.

There is no difference between the reported profits above and their historic cost equivalents.

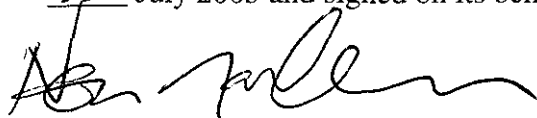
There were no other recognised gains or losses in the year.

The above results relate to continuing operations.

**XRO LIMITED
BALANCE SHEET
AT 31 DECEMBER 2002**

	<i>Note</i>	2002 £m	2001 £m
Fixed assets			
Investments	3	1,571	1,571
Total fixed assets		1,571	1,571
Current assets			
Debtors			
Due after more than one year	4	884	884
Total current assets		884	884
Creditors due within one year		(2)	(2)
Net current assets		882	882
Total assets less current liabilities		2,453	2,453
Creditors due after more than one year	5	(7)	(7)
Net assets		2,446	2,446
Capital and reserves			
Called up share capital	6	172	172
Share premium	7	1,133	1,133
Capital redemption reserve		1	1
Profit and loss account	8	1,140	1,140
Total Shareholders' funds (Including Non-Equity)		2,446	2,446

The Financial statements on pages 5 to 13 were approved by the Board of Directors on 23 July 2003 and signed on its behalf by



N.S. Mackintosh
Director

RECONCILIATION OF MOVEMENTS IN SHAREHOLDERS' FUNDS

	2002 £m	2001 £m
Profit for the financial year	-	450
Dividends proposed and paid (Including Non-Equity)	-	(450)
Net addition to shareholders' funds	-	-
Opening shareholders' funds	2,446	2,446
Closing shareholders' funds	2,446	2,446

SHAREHOLDERS' FUNDS ANALYSED AS FOLLOWS

Equity	2,446	2,446
Non Equity	-	-
	2,446	2,446

NOTES TO THE FINANCIAL STATEMENTS

1. PRINCIPAL ACCOUNTING POLICIES

The Company's major accounting policies are summarised below.

(A) Accounting Principles and basis of preparation

The financial statements are prepared on a historical cost basis and in accordance with applicable United Kingdom Accounting Standards. Accounting policies have been applied consistently in dealing with items which are considered material in relation to the Company's financial statements.

These financial statements have been prepared on a going concern basis. In preparing these financial statements, the Directors have assessed that the Company will continue in operational existence for the foreseeable future and have received a letter of support from Xerox Corporation.

Consolidated accounts have not been prepared as the Company is a wholly owned subsidiary of Xerox Investments Europe B.V., a company incorporated in the European Community, and is therefore exempt under Section 228 of the Companies Act 1985 from the obligation to prepare and deliver group accounts.

Xerox Corporation's Annual Report (Form 10k) has been filed with Securities and Exchange Commission (www.sec.gov).

(B) Investments

Investments in subsidiaries and associates are held at cost, less any provisions required where there has been an impairment in the value of the investments (note 3).

(C) Disclosures

Cash Flow Statement

Under Financial Reporting Standard 1 - Cash Flow Statements, the Company is exempt from the requirement to prepare a Cash Flow Statement.

Related Parties

Under Financial Reporting Standard 8 - Related Party Disclosures, the Company is exempt from the requirement to disclose transactions with other entities within the group headed by Xerox Corporation; other related party disclosures are reported in note 9.

(D) Translation of Foreign Currency

Share Capital is translated at the appropriate historic rate. Differences between historic rates and the balance sheet rate are taken to reserves.

2. PROFITS FOR THE FINANCIAL YEAR AND DIVIDENDS

(A) Profit for the financial year

Directors' remuneration for services provided to the Group as a whole and Auditors' remuneration were borne by a fellow group subsidiary, Xerox Limited. This treatment is consistent with the prior year.

There were no employees of the Company during the year (2001: nil).

(B) Dividends

No dividends were proposed and paid during the year and no final dividends are proposed. In 2001, dividends were proposed and paid of £450m were as follows:

Non-Equity Dividends

- (1) £ 8,867,329 (US\$ 5.54 cents per share) in respect of the 227,552,614 Convertible Cumulative Preference Shares of 1 cent ("the US\$ Cumulative Preference Shares") of the Company.
- (2) £ 440,029,839 in respect of the 1,172,378,553 Preferred Ordinary Shares of 1 cent ("the US\$ Preferred Ordinary Shares") of the Company.

Equity Dividends

- (3) £ 1,102,839 Ordinary Shares of 10 pence ("the Sterling Ordinary Shares") of the Company.

There is no final dividend proposed. Retained result for the year was £ nil (2001: nil).

3. INVESTMENTS

(A) The Company's investment in subsidiaries is analysed as follows

	2002 £m	2001 £m
At 1 January	1,571	1,571
Additions	-	-
At 31 December	1,571	1,571

(B) Principal direct subsidiaries at 31 December 2002, which are intermediate holding companies

	Percentage Voting Interest	Class of Capital owned	Percentage holding
XRI Limited	100%	Ordinary	100%
XRI Limited		5% Pref.	100%
RRXH Limited	100%	Ordinary	100%

All shareholdings are direct except RRXH Limited, 50% of which is held via XRI Limited. All subsidiaries are incorporated in England.

RRXH Limited, through its subsidiary RRXIL Limited, owns 100% of the ordinary share capital of Xerox Limited, Xerox Holding (Nederland) B.V., Xerox XIB Limited (formerly Xerox Investments (Bermuda) Limited) and Xerox XHB Limited (formerly Xerox Holdings (Bermuda) Limited).

A complete list of principal subsidiaries can be found in Xerox UK Holding Ltd's (the ultimate UK parent) financial statements. A complete list of subsidiaries will be filed with the Company's next annual return.

4. DEBTORS - DUE AFTER MORE THAN ONE YEAR	2002	2001
	£m	£m
Amounts due from Group company	884	884

There are no immediate plans to settle this intercompany amount and no interest is charged.

5. CREDITORS - DUE AFTER MORE THAN ONE YEAR

Amounts owed to Group company	7	7
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There are no immediate plans to settle this intercompany liability and no interest is charged.

6. AUTHORISED & CALLED UP SHARE CAPITAL

(A) The Company's share capital

Authorised Share Capital	2002 £000's	2001 £000's
UK Sterling		
2,400,000,000 Ordinary shares of 10p each	240,000	240,000
300,000,000 Convertible Redeemable Preference shares of 20p each	60,000	60,000
2,400,000,000 US\$ Preferred Ordinary shares of 1 cent each (see below)	14,213	14,213
500,000,000 US\$ Convertible Cumulative Preference shares of 1 cent each (see below)	2,945	2,945
	317,158	317,158
US Dollars:		
	\$000's	\$000's
2,400,000,000 Preferred Ordinary shares of 1 cent each	24,000	24,000
500,000,000 Convertible Cumulative Preference shares of 1 cent each	5,000	5,000
	29,000	29,000
Issued and fully paid		
	£000's	£000's
UK Sterling		
1,172,378,553 Ordinary shares of 10p each	117,238	117,238
227,552,614 Convertible Redeemable Preference shares of 20p each	45,512	45,512
US\$ Preferred Ordinary shares (see below)	7,346	7,346
US\$ Convertible Cumulative Preference Shares	1,456	1,456
	171,552	171,552
US Dollars:		
	\$000's	\$000's
1,172,378,553 Preferred Ordinary shares of 1 cent each	11,724	11,724
227,552,614 Convertible Cumulative Preference shares of 1 cent each	2,276	2,276
	14,000	14,000

(B) Rights of shares under the meaning of Accounting Standard FRS4 - Capital Instruments

(i) Sterling Convertible Redeemable Ordinary Preference Shares of 20p each

The shares carry no fixed dividend entitlement. In respect of any dividend declared attributable to Ordinary Preference shares 0.25% is deemed attributable to the Sterling Ordinary shares.

Redeemable by Company at 1p per share between 30th June 2003 and 31st July 2007.

On winding-up the sterling convertible shares confer the right to receive 1p for every 20p in nominal account held. These shares have no voting rights.

(ii) US\$ Preference shares

The convertible Preference share dividend is paid in two equal instalments on 31st January and 31st July at the discretion of the directors.

The Preferred Ordinary shares carry no fixed dividend entitlement. Any dividend declared attributable to Ordinary shares are deemed 99.75% attributable to the US\$ Preferred Ordinary shares.

On winding-up the US \$ preference shares confer the right to receive out repayment in full of the capital paid up on, plus a further amount to 99.75% of the amount available for distribution to members.

Each US \$ Preferred Ordinary share confers the right to 400 votes.

(iii) US\$ Convertible Cumulative

The shares carry no fixed dividend entitlement. On winding-up the Convertible US \$ preference shares confer the right to receive out of the assets of the Company available for distribution to its members in preference to rights of any other shares an amount up to the sum of £1.

No voting rights except on resolutions for winding-up, or variation of capital or if US Preference share dividend is in arrears for six months.

7. SHARE PREMIUM

Of the share premium of £1,133,222,000 reported at 2002 year-end, £604,361,000 arose in 1998, when XRO Limited issued £35,389,000 of ordinary and U.S. \$ preferred ordinary shares at a premium of £604,361,000 to Xerox Overseas Holdings Limited; at the same time XRO Limited increased its investment in RRXH Limited and XRI Limited. The remainder of the share premium arose prior to the 1997 Rank Organisation buyout.

8. PROFIT AND LOSS ACCOUNT

	2002 £m	2001 £m
Balance at 1 January	1,140	1,140
Retained profit for the year	-	-
Balance at 31 December	1,140	1,140

9. RELATED PARTY DISCLOSURE

An overseas subsidiary of the Group, NV Xerox Management Services SA, has provided a loan to a Director of the Company. Throughout the year and at the end of the year there was an outstanding loan to J.F.Lawler of £20,000 (2001: £20,000). No interest was charged on this loan. Mr.J.F.Lawler resigned as a director on 28th of January 2003. The loan to J.F.Lawler was settled as part of his loss of office compensation. No amounts have been provided for or written off against the loan.

10. CONTINGENT LIABILITIES

As a result of the scheme of arrangement following which The Rank Group Plc acquired 100% of the issued share capital of The Rank Organisation Plc in 1996, it is possible that further liabilities other than those provided for in these accounts may arise. No provision has been made for these liabilities at 31 December 2002 as, in the opinion of the Directors, it is unlikely that they will occur.

The Company had no other contingent liabilities at 31 December 2002 (2001: nil).

11. ULTIMATE PARENT COMPANY

The ultimate parent company, ultimate controlling party and the largest group in which the results of XRO Limited are consolidated is that of Xerox Corporation, which is incorporated in the United States of America. Copies of the Xerox Corporation Annual Report and Accounts may be obtained from The Investor Relations Department, Xerox Corporation, 800 Long Ridge Road, PO Box 1600, Stamford, Connecticut 06904, U.S.A.; World Wide Web <http://www.xerox.com>.

The smallest group in which the results of XRO Limited are consolidated is that of Xerox Investments Europe BV, which is registered in The Netherlands. Copies of the Xerox Investments Europe BV Annual Report and Accounts are available from Xerox Investments Europe BV, Gondel 1, 1186 MJ Amstelveen, The Netherlands.

Directors' Responsibilities

Company law requires the Directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and of the profit or loss for that year. The Directors confirm that:

- suitable accounting policies have been selected and applied consistently;
- *reasonable and prudent judgements and estimates have been made;*
- applicable accounting standards have been followed; and
- the financial statements have been prepared on the going concern basis;

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

Independent Auditors Report

Independent Auditors' report to the members of XRO Limited

We have audited the financial statements, which comprise the profit and loss account, the balance sheet, reconciliation of movements in shareholders' funds and the related notes which have been prepared under the historical cost convention and the accounting policies set out in the statement of accounting policies.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report and the financial statements in accordance with applicable United Kingdom law and accounting standards are set out in the statement of directors' responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards issued by the Auditing Practices Board. This opinion has been prepared for and only for the company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or in to whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the financial statements 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 financial statements, 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 is not disclosed.

Basis of audit opinion

We conducted our audit in accordance with auditing standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, 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 financial statements 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 financial statements.

Opinion

In our opinion the financial statements give a true and fair view of the state of the company's affairs at 31 December 2002 and of its retained result for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

PricewaterhouseCoopers LLP
PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
Uxbridge

23 July 2003