

NORTHERN POWERGRID (NORTHEAST) LIMITED

REGISTERED NUMBER 02906593

REGULATORY ACCOUNTS

FOR THE YEAR ENDED

31 MARCH 2016

NORTHERN POWERGRID (NORTHEAST) LIMITED

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for the Year Ended 31 March 2016**

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NORTHERN POWERGRID (NORTHEAST) LIMITED

REGISTERED NUMBER 02906593

Registered Office: Lloyds Court, 78 Grey Street, Newcastle upon Tyne, NE1 6AF

The directors present the Regulatory Accounts for the year ended 31 March 2016 (the "Regulatory Year") of Northern Powergrid (Northeast) Limited (the "Company"), which include the Strategic Report, Directors' Report, Corporate Governance Statement and audited financial statements for that year. The businesses of the affiliates of the Company that have carried out activities forming part of, or ancillary to, the distribution business of the Company have not been consolidated with the activities of the Company in the preparation of these accounts. The Regulatory Accounts are separate to and, therefore, may differ from the statutory financial statements of the Company for the year ended 31 December 2015, which were drawn up and presented in accordance with the Companies Act 2006.

Cautionary statement regarding forward-looking statements

The Regulatory Accounts have been prepared in accordance with Part A of standard condition 44 (Regulatory Accounts) of the electricity distribution licence granted to the Company by the Secretary of State (the "Licence"). The Company, its directors, employees or agents do not accept or assume responsibility to any other person in connection with this document, other than in respect of the obligations imposed on the Company by standard condition 44 of the Licence, and any such responsibility or liability is expressly disclaimed. The Regulatory Accounts contain certain forward-looking statements, which can be identified by the fact that they do not relate only to historical or current facts. In particular, all statements that express forecasts, expectations and projections with respect to future matters, including trends in results of operations, business prospects, the availability of financing to the Company and anticipated cost savings are forward-looking statements.

By their nature, these statements and forecasts involve risk and uncertainty because they relate to events and depend on circumstances that may or may not occur in the future. There are a number of factors that could cause actual results or developments to differ materially from those expressed or implied by these forward-looking statements and forecasts. The forward-looking statements reflect the knowledge and information available at the date of preparation of the Regulatory Accounts and will not be updated during the year. Nothing in the Regulatory Accounts should be construed as a profit forecast.

STRATEGIC REPORT FOR THE REGULATORY YEAR

The Company is an authorised distributor under the Electricity Act 1989, holds an electricity distribution licence granted by the Secretary of State and is part of the Northern Powergrid Holdings Company group of companies (the "Northern Powergrid Group"). As a distribution network operator ("DNO"), the Company distributes electricity to approximately 1.6 million customers connected to its electricity distribution network within its distribution services area in the northeast of England, which extends from North Northumberland, south to York and west to the Pennines, and distributed some 14,862 GWh of electricity to those customers during the Regulatory Year. The Company's distribution network includes over 41,000km of overhead and underground cables and over 27,000 substations of all types and receives electricity from generators connected directly to it and from the National Grid's transmission system and distributes that electricity at voltages of up to 132kV.

The main classes of asset, which make up the Company's distribution network, include:

<u>Asset class</u>	<u>Approximate number</u>
Total circuit length (underground and overhead)	41,013 kilometres
Ground-mounted distribution substations	11,207
Pole-mounted distribution substations	16,172
Major substations	256
LV services (overhead)	151,782
LV services (underground)	1.45 million

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STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

In common with the Northern Powergrid Group, the Company operates a business model and strategy based on its six core principles (the "Core Principles"), which are:

Principle	Strategy	Indicator
Financial strength	Effective stewardship of the Company's financial resources, investing in assets and focusing on long-term opportunities, which contribute to the Company's future strength.	Profitability, cash flow and maintenance of investment grade credit ratings.
Customer service	Delivering reliability, dependability and exceptional service.	Improving network resilience and performance, measured by: customer minutes lost, customer interruptions and customer satisfaction.
Operational excellence	Setting high standards for the Company's operations, system investment and maintenance.	Effective asset management, managing commercial risk and improving network resilience and performance.
Employee commitment	Equipping employees with the resources and support they need to operate successfully and in a safe and rewarding work environment.	Leading safety performance, engaging employees and effective leadership.
Environmental respect	Using natural resources wisely and protecting the environment, where it is impacted by the Company's operations.	Reducing environmental impact and promoting and pursuing long-term sustainability.
Regulatory integrity	Adhering to a policy of strict compliance with applicable laws, regulations, standards and policies.	Strong internal controls, regulatory engagement and industry influence.

Strategic objectives

The Company's strategic objectives are based on the Core Principles, remain consistent and are to build a business, which:

- continues to generate value over the long-term;
- invests in and manages its electricity distribution network in an efficient and effective manner;
- provides its customers with an excellent standard of service;
- engages with its employees so that they feel rewarded and recognised as part of a team that sets and achieves increasingly high standards of performance; and
- is viewed as being a leader in shaping the future direction of the electricity distribution sector in the United Kingdom.

As part of its strategy the Company continues to be committed to putting safety first, respecting its customers, their time and property, doing a quality job, responding effectively to major incidents on the network in times of severe weather and caring for its local environment.

STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

REVIEW OF THE REGULATORY YEAR

The Company delivered a satisfactory financial performance for the Regulatory Year, which benefited from a further change to the rate of taxation and continued effective cost control, with revenue at £327.5 million being £45.3 million less than in the regulatory year ended 31 March 2015. The decrease in revenue was mainly due to the reduction in tariffs introduced with effect from the start of the current regulatory period, which runs from 1 April 2015 to 31 March 2023 and is known as ED1.

Having been given permission by the Competition and Markets Authority (the "CMA") to appeal against the licence modifications that gave effect to the ED1 price control, one of the main priorities for the Company in the Regulatory Year was to take forward that appeal, which related to three specific areas:

- (i) Ofgem's decision to demand further cost savings in relation to smart grid technology over and above the ones proposed by the Company and captured in Ofgem's original cost benchmarking exercise;
- (ii) Ofgem's assessment of the variation in wage rates across the country; and
- (iii) Ofgem's projections for labour cost increases.

On 29 September 2015, the CMA published its final determination in respect of the Company's appeal and upheld one ground of the appeal in respect of the adjustments made by Ofgem to reflect potential savings available from the introduction of smart grids and other technological innovations, because Ofgem's decision was not based on robust evidence. The CMA's determination will increase the Company's cost allowances over ED1 by approximately £16 million, in 2012/2013 prices, which affects the Company's projected regulatory asset value at the end of ED1 as well as its allowed revenues within ED1. The CMA did not uphold the Company's other two grounds of appeal, deciding that Ofgem's decision fell within the margin of discretion that is available to it in respect of such matters and the Company's case fell short of demonstrating that Ofgem's decision was wrong.

British Gas Trading Limited ("British Gas") was also granted permission to appeal the price control and appealed on six grounds. The CMA agreed with British Gas in part on one of those grounds only, resulting in an adjustment to part of the price control that adjusts the overall level of revenue a DNO can earn by providing a reward in proportion to the extent to which Ofgem agrees with the DNO's cost forecasts. The outcome of British Gas' appeal was a reduction of approximately £6 million in the Company's allowed additional income in ED1 in 2012/2013 prices. The net effect of the two appeals on the Company's allowed revenues in ED1, excluding the uplift on the Company's projected regulatory asset value at the end of ED1, is a reduction of approximately £2 million in 2012/2013 prices.

The Company continued with its policy of investing efficiently in its electricity distribution network during the Regulatory Year, investing £185.7 million, a reduction on its largest ever capital expenditure programme of £217.5 million delivered in the regulatory year ended 31 March 2015.

Improving customer satisfaction remained a management priority for long-term improvement and, during the Regulatory Year, the Company introduced the new Customer Relationship Management ("CRM") system, which will provide quicker and more accurate information to customers and improve the effectiveness of the customer complaints process. The Company continues to be one of the industry leaders in terms of social obligations and stakeholder engagement, and was again ranked second among the DNOs in respect of its annual stakeholder engagement submission to Ofgem.

The Company beat Ofgem's targets for the quality of the electricity supply provided to its customers and continued to focus on reducing the average times taken to restore supplies following a power cut. In that respect, the Company's adoption of an Operations model based on a number of locally-focussed industrial, rural and urban zones, has begun to deliver improvements in the Company's response to unplanned power cuts following the introduction of a new guaranteed standard for the restoration of supply within 12 hours of a power cut occurring from 1 April 2015 onwards.

STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

REVIEW OF THE REGULATORY YEAR (CONTINUED)

Environmental performance for the year to 31 December 2015 continued to be strong with incidents reportable to the Environment Agency being better than target. However, oil spills and leaks from the Company's assets and SF₆ gas discharges from electrical plant exceeded target, which was slightly disappointing as the Company had delivered its most successful annual environmental performance in 2014. Given the impact on the environment of such events, the Company remains committed to reducing losses from fluid-filled cables and, during ED1, plans to replace a significant number of those assets on a phased and prioritised basis, and to increase the use of perfluorocarbon tracers to improve the efficiency of oil leak identification.

The Company's safety performance continued to be strong, with an Occupational Safety and Health Administration ("OSHA") rate of 0.21 being recorded for the year to 31 December 2015 (2014: 0.1), such that it made an effective contribution to the Northern Powergrid Group equalling its best ever safety performance, and the long-term trend in the Company's overall safety performance continued to compare well with that of the industry. The Company beat its internal targets in respect of restricted duty and medical treatment accidents and preventable vehicle accidents but missed its targets in respect of lost time accidents and operational incidents.

CORE PRINCIPLES

Financial strength

During the Regulatory Year, the Company continued to maintain good control in respect of both its capital and operating costs by effectively managing the various financial risks that could have had an adverse impact on its business.

The ED1 price control, as amended following the outcomes of the appeals to the CMA, provides the Company with stability in terms of its income until 31 March 2023. The ED1 price control has been set for eight years with provision for a mid-period review of the outputs that the Company is required to deliver and, in that respect, the Company recognises that it needs to continue to show that it is delivering reliable services to its customers, while operating in an efficient and effective manner.

Key aspects of financial performance for the Regulatory Year were as follows:

Revenue

The Company's revenue at £327.5 million was £45.3 million lower than the prior year mainly due to the reduction in tariffs introduced with effect from the start of ED1.

Operating profit and position at the Regulatory Year end

The Company's operating profit at £143.3 million was £39.6 million lower than the previous year, primarily reflecting decreased revenues and higher depreciation charges, partly offset by lower grid exit charges. The statement of financial position on page 37 shows that, as at 31 March 2016, the Company had total equity of £843.2 million. The directors consider the Company to have a strong statement of financial position which, when coupled with the preference of its parent company, Berkshire Hathaway Energy Company ("Berkshire Hathaway Energy"), for operating with lower levels of debt than equivalent companies in the sector, creates a stable base for continued strong performance during ED1.

Finance costs and investments

Finance costs net of investment income at £27.0 million were £1.2m higher than the prior year due to higher net borrowings including a new credit facility with the European Investment Bank (the "EIB") from 16 December 2015 (see debt structure below).

Taxation

The effective tax rate in the year was 8.3%. The effective tax rate before adjusting for the impact of the changes in tax rates by the Finance Act 2015 would be 17.0%. Details of the income tax expense are provided in Note 9 to the Regulatory Accounts.

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STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

CORE PRINCIPLES (CONTINUED)

Financial strength (continued)

Results and dividends

The Company made a profit after tax for the year of £107.0 million (2014: £125.2 million). An interim dividend of £20.6 million was paid during the Regulatory Year (2015: £30.0 million) and the directors recommended that no final dividend be paid in respect of the year to 31 December 2015.

Share capital and debt structure

There were no changes to the Company's share capital during the Regulatory Year. On 2 December 2015, the Company entered into an agreement with the EIB, which provided the Company with a credit facility of £120 million. The financial obligations of the Company under this agreement are guaranteed by Northern Powergrid Holdings Company and, on 16 December 2015, the Company drew on the credit facility in its entirety at a fixed rate of 2.564% for a period of 12 years.

Dividend policy

The Company's dividend policy is that dividends will be paid only after having due regard to available distributable reserves, available liquid funds and the financial resources and facilities needed to enable the Company to carry on its business for at least the next year. In addition, the level of dividends is set to maintain sufficient equity in the Company so as not to jeopardise its investment grade issuer credit rating.

Cash flow

The Company aims to collect from customers and pay suppliers within contracted terms. Any surplus cash held is remitted to Yorkshire Electricity Group plc ("YEG"), a company in the Northern Powergrid Group, and invested accordingly, generating a market rate of return for the Company.

Movements in cash flows were as follows:

Operating activities: Cash flow from operating activities at £142.6 million was £18.0 million lower than the previous year, mainly as a result of lower operating profits partially offset by favourable working capital movements.

Investing activities: Net cash used in investing activities at £155.7 million was £16.2 million lower than the previous year, reflecting higher receipt of customer contributions.

Financing activities: The net cash from financing activities at £13.1 million represents a £1.8 million favourable variance compared to the previous year, reflecting net movements in borrowings required to fund business operations in the year.

Liquidity risk

As at 31 March 2016, the Company had access to £75 million under a five-year committed revolving credit facility provided by Lloyds Bank plc, The Royal Bank of Scotland plc and Abbey National Treasury Services plc. The revolving credit facility was due to expire on 20 August 2017 but, on 30 April 2015, the facility was restated and amended and is now due to expire on 30 April 2020. The Company expects to raise further facilities, as required, at that time.

In addition, the Company has access to further short-term borrowing facilities provided by YEG and to a £19 million overdraft facility provided by Lloyds Bank plc, which is reviewed annually.

The directors do not consider there to be any doubt over the Company's ability to raise appropriate levels of finance in the future, given its investment grade issuer credit rating and the fundamental financial strength and nature of its business.

Interest rate risk

The Company is financed by long-term borrowings at fixed rates and has access to short-term borrowing facilities at floating rates of interest. As at 31 March 2016, 100% of the Company's long-term borrowings were at fixed rates and the average maturity for these borrowings was 13 years.

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STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

CORE PRINCIPLES (CONTINUED)

Financial strength (continued)

Currency risk

No material currency risks are faced by the Company.

Pensions

The Company is a participating employer in the Northern Powergrid Group of the Electricity Supply Pension Scheme (the "Scheme"), a defined benefit scheme. Full details of the Company's commitments to the Scheme and the associated deficit repair payments are provided in Note 23 to the Regulatory Accounts.

The Company also participates in the Northern Powergrid Pension Scheme, which is a defined contribution scheme.

Insurance

As part of its insurance and risk strategy, the Northern Powergrid Group has in place insurance policies, which cover risks associated with employers, third party motor and public liability. The Northern Powergrid Group carries appropriate excesses on those policies and is effectively self-insured up to the level of those excesses. Consequently, the risk management and health and safety programmes in place are viewed as extremely important elements of the business, given the contribution they make to the elimination or reduction of exposure to such risks.

Customer service

During the Regulatory Year, the Company distributed electricity to customers in its distribution services area and continued to improve the overall performance of the distribution network through an investment strategy targeted at delivering improvements in an efficient and cost-effective manner. The Company remains focused on delivering a reliable and dependable supply of electricity, together with a high standard of service to its customers.

Customer service improvements are a priority for the Company, which has been consistently ranked in the lower half of Ofgem's customer service tables. The Company has a long-term goal to improve this ranking and has a programme of actions in place to support improvements to the customer experience.

Customer satisfaction with the Company's response to unplanned power cuts showed gradual improvement in the Regulatory Year and the focus remains on improving restoration times and proactively communicating more timely and accurate information to customers. Enhancements were made to the interactive voice response telephony system throughout the Regulatory Year to make it easier for customers to talk to a customer service advisor if they so wish. Customer satisfaction with planned power cuts also showed some encouraging improvement with the Company improving the design of written customer communications and providing a text and email service to remind customers 72 hours and then 24 hours ahead of the power cut taking place.

The Company has invested in improving the reliability of under-performing parts of the distribution network by continuing to identify "hot spots" of particularly poor network performance and taking specific action to address the issues in those areas. In the customer service support areas, further investment has been directed towards information technology with the introduction of the new CRM system to improve the self-service offering and provide quicker and more accurate information to customers with workflows automatically routed within both the Company and its contractors. This technology will enable customers to communicate with the Company in a range of accessible and easy ways across several channels.

STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

CORE PRINCIPLES (CONTINUED)

Customer service (continued)

The Company has built on the industry-leading communications and engagement approaches used to support its business plan and maintains a number of engagement channels. Independently chaired expert panels continue to play a key role in challenging the Company's plans, monitoring its performance and helping to deliver innovative initiatives and services. Guided by these panels, the Company has been able to direct effort towards public meetings in the operating zones, community energy workshops aimed at enhancing the take-up of low-carbon technologies and wider collaborations such as with other utilities via Infrastructure North. The feedback received as part of the stakeholder engagement process helped the Company to further develop its customer experience improvement programme.

The Company recognised that the evolving nature of the environment and the level of customer service provided in respect of new connections to the network required additional focus and, as such, initiated a review of this area of the business. Further details regarding the connections activity in the Regulatory Year are provided under "Connections to the network" below.

In common with other DNOs, the Company is actively engaged in the national project, which has created a single national three-digit emergency number for power cut calls, and is leading three of the four sub-groups within the project. Following a consultation, Ofcom agreed that there was a strong case for that three-digit number to be introduced and announced in June 2015 that the number was to be 105. The number is scheduled to go live in 2016.

The performance of the DNOs against guaranteed standards, which are set for activities such as restoring supplies after power cuts, provides a measure of the level of customer service and Ofgem's incentive scheme for quality of service, by which the DNOs are provided with financial incentives, is based upon targets set by Ofgem with regard to each DNO's performance.

Customer minutes lost ("CML") and customer interruptions ("CI") are the key performance indicators used by the Company to measure the quality of supply and system performance. CML measures the average number of supply minutes lost for every connected customer due to both planned and unplanned power cuts that last for three minutes or longer. CI measures the average number of supply interruptions for every 100 connected customers due to planned and unplanned power cuts that last for three minutes or longer.

In respect of these key customer service performance indicators, the goal is to achieve performance that is below Ofgem's target number in respect of CML and CI. The Company's currently reported performance for the Regulatory Year is as follows:

	Year to 31 March 2016		Year to 31 March 2015	
	Actual	Target	Actual	Target
CML	49.7	65.9	56.1	70.6
CI	58.2	63.8	65.3	68.1

Consequently, performance in the Regulatory Year was better than Ofgem's target for both CML and CI and contributed to the Company's improved customer service performance.

In May 2015, the Company put forward its stakeholder engagement submission to Ofgem in respect of its work during the Regulatory Year. This included initiatives such as expanding the role of digital solutions in providing customer services and the enhancement of the Company's relationship with some voluntary sector organisations, with which it works closely in developing and delivering certain services particularly in respect of those customers on the Company's priority services register.

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STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

CORE PRINCIPLES (CONTINUED)

Customer service (continued)

Having presented its submission to Ofgem's panel, the Company maintained its position as the second placed DNO group. A reward of £0.9 million was secured, which will be received during the regulatory year ended 31 March 2017, and the Company intends to reinvest its reward in initiatives that will continue to build on this strong stakeholder engagement performance.

Under the Broad Measure of Customer Satisfaction, an independent market research company carried out telephone surveys with the Company's customers to find out how satisfied they were with the services provided. During the Regulatory Year, surveys were carried out of a number of customers who had contacted the Company regarding an unplanned or a planned power cut, had requested a price quotation and a subsequent connection, or had a general enquiry where a service had been provided or a job completed. The Company recorded an overall satisfaction score of 84.1% for the Regulatory Year (2015: 81.9%) and expects that the customer service improvement plan, including the range of initiatives noted on pages 6 and 7, will improve the services provided to customers and so increase the satisfaction ratings year-on-year.

While recognising that its customer service performance can be improved, the Company continued to make steady progress during the Regulatory Year with customer satisfaction scores generally improving, performance to reduce service failures meeting target, the connections customer service improvement plan being delivered and its social obligations and stakeholder engagement activity continuing to be among the leading in the industry.

Connections to the Network

During the Regulatory Year, the Company continued to deliver its action plans to improve the connections services provided to its customers, whilst also actively facilitating the development of competition from independent connections providers ("ICPs"). The Company continued to engage regularly with its connections customers in groups and individually, holding monthly customer surgeries, twice yearly customer stakeholder events and contributing to national stakeholder forums and events.

There were three main areas of development in the Company's connections business during the Regulatory Year with the introduction of the new Competition in Connections Code of Practice, compliance with which became a licence condition with effect from the end of October 2015, introduction of the full Incentive on Connections Engagement ("ICE") regime in April 2015 and introduction of a customer service improvement programme to deliver improvements in customer satisfaction for small works customers. The customer satisfaction improvement programme continued to be delivered in the first quarter of 2016, is focussed on actions derived from customers' feedback obtained from the weekly telephone surveys and is designed to support the Company's goal to be the leading provider of customer service within the electricity distribution sector.

The Company participated with other DNOs in the development of the new Competition in Connections code of practice and implemented the required new processes, including the provision of dual quotations, enabling ICPs to self-determine and approve points of connection to the network, and simplifying the authorisation process for ICPs' operational staff.

The start of ED1 saw the introduction of ICE in respect of customers requiring larger connections to the network, so that the needs of those customers can be met more effectively. Under ICE, the Company is required to submit a customer service improvement work plan for the forthcoming regulatory year at the end of April, followed by a comprehensive 'looking back and forward' report commenting on the actions delivered in the previous year and future actions proposed in the service improvement plan. The Company worked throughout the Regulatory Year to deliver those actions and continued to engage actively with customers through both informal and formal stakeholder events.

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STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

CORE PRINCIPLES (CONTINUED)

Customer service (continued)

Corporate responsibility

The Company values its relationship with its customers and other stakeholders and recognises the importance of maintaining a secure and safe power supply for its customers and their local communities. That commitment is underpinned by five customer promises, which are to put safety first, to respect the Company's customers, their time and property, to do a really good job, to be there when needed and to care for the local environment.

The Company maintained its key partnerships with the Environment Agency, the local authorities and the local resilience forums so that it can respond quickly to significant faults on, or threats to, the network. The Company has well-established emergency procedures that are implemented when customers are without power for some time and, as such, the Company responded well to the significant weather-related incidents, including Storms Desmond, Eva and Gertrude, which impacted on its electricity distribution network during the Regulatory Year.

The Company utilises its 'customer ambassadors' and customer liaison officers, who are allocated to each of its operating zones, to address customers' concerns and resolve their complaints, and works with the British Red Cross to pay particular attention to the welfare of customers on the priority services register so that those customers are kept informed of the situation throughout the event and after the power has been restored.

The Company continued to focus on some of its more vulnerable customers and works closely with them and the organisations that represent them to improve how it communicates and provides support. The Northern Powergrid Group's social issues expert group focusses on that area and also on how service improvements for priority services customers can be identified and prioritised. The Company conducted a campaign aimed at encouraging eligible customers to join and to raise awareness of the priority services register by promoting the benefits of being on the register more widely, such that the quality of the information held on the register and the services offered to priority services customers continued to improve.

The Northern Powergrid Group has in place a small programme, from which donations were made during the Regulatory Year to charities nominated by the top three teams in its "Safety Champions" initiative, which is aimed at supporting improvements in safety performance in the operational zones.

Safety remains the Company's first priority and underpins all operations. During the Regulatory Year, the Company continued to deliver its regular series of school safety presentations and, alongside other key organisations, participated in 'Crucial Crew', which is a schools-based safety initiative that teaches children to recognise and avoid situations that put them in danger, with those initiatives reaching thousands of pupils.

Other initiatives during the Regulatory Year included Make the Grade in Energy, an education, skills and employability programme, support for community energy groups, Energy Heroes, a new educational programme, which uses the maths curriculum at primary school level to promote awareness of energy costs and ways of saving energy, and Green Doctors, a multi-partner project which helped to install energy saving measures and give advice to fuel poor households.

Operational excellence

The Company's core service continues to be providing and maintaining an efficient distribution network that delivers electricity effectively. During the Regulatory Year, £185.7 million was invested in the improvement of the distribution network, a reduction on the £217.5 million invested in the previous year.

STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

CORE PRINCIPLES (CONTINUED)

Operational excellence (continued)

The Company's continued and substantial investment in its distribution network has seen reliability increase over a sustained period and the Company has generally outperformed the targets set by Ofgem in respect of CI and CML. The Company's inspection and maintenance regimes have ensured that the underlying health of the network assets has been sustained and none of the leading indicators used by the Company suggest any diminishing performance in this respect in the future.

Operational activity

The Company continued to implement its approved network investment strategy, which is designed to deliver improvements in an efficient and cost-effective manner in order to improve the network's resilience. The Company is committed to enhancing the reliability of the network such that fewer power cuts affect customers and, when power cuts do happen, they are shorter in duration.

The Company's Operations structure is designed to respond effectively to the needs of customers and local communities by delivering improved performance standards in the restoration of power following power cuts and in new connection activities for small works. That structure is organised into operating zones around the main conurbation of Tyne & Wear, the industrialised area around the Tees and the rural areas of Northumberland, Durham and North Yorkshire, including the Dales, the Vale of York and the North Yorkshire Moors. As a new guaranteed standard for the restoration of supply within 12 hours of a power cut occurring came into effect from 1 April 2015, the Company's operational structure will provide a more localised focus and, therefore, improved response times in the event of a power cut.

During the Regulatory Year, the Company invested in technology to support its drive to improve response times, including the automated power restoration system ("APRS") which operates within the existing network management system. In the event of a high-voltage fault, APRS analyses the information presented by intelligent assets installed on the network and, from that information, determines where the fault is located and executes switching to restore power to the 'healthy' network in a safe manner in under three minutes. APRS was operated initially in advisory mode, allowing intervention in the process to verify the outcome, and was successfully transitioned to live mode in a controlled manner, such that it is planned to enable APRS at some 306 primary substations across the Northern Powergrid Group by the end of ED1. The Company expects, therefore, that APRS will significantly improve the service to customers due to the speed with which it can understand the information presented and then complete the switching required to restore power.

The Company responded well to the major weather events that impacted its network during the Regulatory Year, the most significant being the extensive lightning and wind storm of 1 July 2015, the high winds that affected the northern Pennines and Northumberland during Storm Desmond in early December, the flooding that occurred as a result of Storm Eva on 26 and 27 December 2015 and the high winds during Storm Gertrude on 29 January 2016, which resulted in the Company invoking its major incident management plan on each occasion.

The high winds during Storm Desmond continued for some 39 hours damaging the overhead network and preventing working at height for that time. However, once the high winds subsided, the fault repair and supply restoration performance was effective in restoring power to the affected customers without undue further delay. Storm Gertrude mainly affected Northumberland, Tyne and Wear and County Durham and resulted in some 25,000 customers being affected by power cuts, with 98% of those customers having their power restored within 12 hours and 82% within three hours.

The flooding caused by Storm Eva impacted properties in North Yorkshire, with York City Centre significantly affected. However, the Company's investment in flood defences at its Melrosegate and Foss Island substations and in high capacity pumping equipment meant that supplies to the vast majority of the approximately 66,000 premises connected to those substations were maintained throughout the storm. Following Storm Eva, the Company instigated a programme of work to inspect flooded homes and businesses, to replace service cables and equipment, where required, and to inspect equipment located in the affected areas including substations, link boxes and feeder pillars.

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STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

CORE PRINCIPLES (CONTINUED)

Operational excellence (continued)

Operational activity (continued)

The Company's priorities during the Regulatory Year included delivering a significant level of capital expenditure on the network as in the previous year, a further reduction in the average level of fault repair work in progress, a robust approach to the control of operations on the low-voltage network and continued focus on the restoration times associated with both high and low-voltage power cuts, with high-voltage restoration performance averaging some 57.6 minutes (2015: 55.6 minutes), after allowing for severe weather incidents and other exemptions.

The Company undertook various major projects during the Regulatory Year in support of those targets and as part of the investment strategy, including:

- Completion of a major reinforcement project in the Knaresborough area culminating in the commissioning of the new Knaresborough 132kV switching station;
- Completion of 66kV circuit breaker replacement works at North Tees, Fossway, Toronto and Linton and replacement of primary switchgear at Catterick and three transformers at North Tees;
- Continuation of reinforcement works in the Harrogate and Potterhouse areas and remediation of fault-level issues at Foss Island by replacing both transformers and reconfiguring the network in the area;
- Refurbishment of 143 132kV overhead line towers and 368 EHV overhead line towers and replacement of approximately 200 EHV poles as part of circuit refurbishment works or individually, based on their condition;
- Commencement of works to replace a substantive part of the overhead tower line between Malton, Thornton Dale and Whitby with underground cables;
- 147km of high-voltage overhead line and 94km of low-voltage overhead line was rebuilt and/or refurbished;
- 15 units of high-voltage outdoor switchgear, 35 high-voltage distribution substations and 225 units of high-voltage indoor switchgear were replaced; and
- 298 new remote control points were installed and commissioned.

In order to deliver its investment strategy, the Company undertook its activities using a mix of its own staff and contractors, including affiliated companies in the Northern Powergrid Group.

Employee commitment

Health and safety

The focus on health and safety continued to be of paramount importance for the directors, as it is for all employees. There is a continuous drive for improvement in safety performance through the setting of challenging goals and the pursuit of a comprehensive safety and health improvement plan, which reflects the Company's fundamental objective that every employee and contractor should go home at the end of each shift uninjured and in good health after a productive day's work.

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STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

CORE PRINCIPLES (CONTINUED)

Employee commitment (continued)

Health and safety (continued)

The Company makes no compromise in respect of its health and safety obligations and centres its safety plans and systems on the principles found in companies with world class safety performance. The Company's safety record over a number of years suggests that it is one of the safest in the sector in which it operates and it will strive to improve performance still further and, in doing so, maintain its position over the coming years. Having identified issues that may pose an increased safety risk, such as metal theft and the roll-out of smart meters, the Company is implementing various measures through its safety and health improvement plan that will build incrementally on the existing strong safety record and ensure that safety considerations are always part of the investment decision-making and appraisal process.

The Company measures its health and safety performance in calendar years and operational incident performance for the year ended 31 December 2015 was disappointing with the number of switching issues experienced on the high-voltage network resulting in eight such incidents occurring in the year against a target of five. As one of the key deliverables in the Company's safety and health improvement plan is to raise awareness and improve the concentration skills of its operational engineers and other employees, the Company increased its operational audit rate of senior authorised persons such that the operational practices of all the senior authorised persons were verified during 2015. The Company also delivered operational seminars, stand down briefings, and regular safety newflashes to staff in order to cascade information on safety trends, issues and incidents.

The Company's safety and health improvement plan targets continuous improvement and delivery of the various initiatives contained in that plan contributed to the Company recording an OSHA rate for 2015 of 0.21 (2014: 0.1) against a target of 0.32.

The Company uses several key performance indicators to monitor safety performance, with the goal of achieving performance that is below the target number. The main key performance indicators are as follows:

	2015		2014	
	Target	Actual	Target	Actual
Lost time accidents	1	2	1	1
Restricted duty accidents	1	0	1	0
Medical treatment accidents	1	0	1	0
Operational incidents	5	8	5	5
Preventable vehicle accidents	10	9	11	10

The Company experienced two lost time accidents in 2015 as opposed to one in 2014 and did not record any medical treatment or restricted duty cases. In addition, performance in respect of preventable vehicle accidents was one accident below the target for the year and showed an improvement compared with 2014. Consequently, the Company made a strong contribution to the Northern Powergrid Group equalling its best ever safety performance and the long-term overall trend continued to compare well with that of the industry. None of those incidents gave rise to any significant safety-related risks.

In common with the Berkshire Hathaway Energy group, the Northern Powergrid Group measures its safety performance in terms of the OSHA rate, which is a measure used in the United States to capture safety incidents down to minor levels of medical treatment, such as a stitch or the use of prescription pain killers. As part of its plan to reduce the OSHA rate across the group, Berkshire Hathaway Energy issues daily e-mail updates in respect of performance against its overall OSHA rate and preventable vehicle accident targets, which include information on incidents that have occurred. The Company's Director of Safety, Health and Environment also delivered updates using conference call facilities, which were available to the entire workforce, regarding performance and other safety-related issues.

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STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

CORE PRINCIPLES (CONTINUED)

Employee commitment (continued)

Health and safety (continued)

Delivery of the various initiatives in the safety and health improvement plan also contributed to the Northern Powergrid Group achieving an OSHA rate of 0.26 against a target of 0.35, which equated to only six recordable incidents and equalled the best ever performance recorded in 2014.

As part of the safety and health improvement plan and in order to reinforce the operational safety values, the Company continued to implement its cross-business operational assurance audit programme and its senior management field engagement programme in order to improve two-way communication on safety and other key business issues. The Company continued to implement a robust road risk management plan, which involved electronic driving licence checking, delivering road risk awareness workshops to new employees and using risk reduction tools such as online driver assessment and training followed by an on-road refresher training session if required. The driver training programme provides practical driving training to a targeted population of drivers and is the primary route to improving driver skills in the longer term. Recognising that driving is one of most hazardous activities undertaken on a daily basis, the programme was expanded further throughout 2015 via an interactive, web-based system designed to assess skills and then provide individual training plans to improve hazard perception and reinforce specific aspects of driving-related skills. The Company also commenced a programme to install a telematics system in all of its fleet vehicles in order to support driver and vehicle safety by encouraging responsible and safe driving styles, assist with the completion and management of vehicle safety checks, and expedite investigation of vehicle accidents and incidents.

During the Regulatory Year, the Company received an Order of Distinction Award from the Royal Society for the Prevention of Accidents for achieving 15 consecutive Gold Awards in recognition of achievements in 2015 and for continued or improving standards of health and safety over a sustained period. The Company's health and safety management systems were subject to the regular bi-annual external surveillances and, on conclusion of those assessments, the auditor recommended that the Company maintained its OHSAS 18001 accreditation.

The sickness absence rate across the Northern Powergrid Group for 2015 was 2.71% (2014: 2.32%), which was an increase on that experienced in 2014 but does not give rise to any particular cause for concern.

Management structure

Operational management of the Company and that of its affiliate, Northern Powergrid (Yorkshire) plc ("NPg Yorkshire"), is undertaken by a single senior management team with specific functional responsibilities. Those functional responsibilities are in respect of operations, health, safety and environment, asset management (including procurement), customer service, business development (including new connections to the network), policy and markets (including trading and innovation), regulation, human resources, organisation development, legal and finance (including property management, stakeholder engagement and information technology). Some of those functions also provide services across the Northern Powergrid Group.

Employees

The Company continued to apply appropriate control to its headcount policy and to place significant emphasis on the importance and application of high standards of management and performance in support of the Core Principles. The Company ensures that a level of consistency is adopted in so doing and, in respect of employee relations, continued to build constructive and partnered relationships with the trades unions. In that respect, the Company has or is working towards securing multi-year pay agreements with the various employment groups such that the relevant terms and conditions are fair and appropriate across the Northern Powergrid Group.

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STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

CORE PRINCIPLES (CONTINUED)

Employee commitment (continued)

Employees (continued)

In addition, the Northern Powergrid Group will continue to recruit trainees under its workforce renewal programme during ED1 taking account of the rate at which existing employees either leave or retire from the Northern Powergrid Group. During the Regulatory Year, the Northern Powergrid Group recruited a total of 154 members of staff, of which 93 were part of the workforce renewal programme. In addition, 70 trainees who were part of the workforce renewal programme in previous years graduated from their training programmes.

As a member of the Berkshire Hathaway, Inc. group of companies, Berkshire Hathaway Energy sets high expectations for honesty and integrity in the conduct of all business activity. Consequently, the Company is committed to proper business conduct and has adopted the Berkshire Hathaway Energy code of business conduct, which details the commitment to ethics and compliance with the law, provides reporting mechanisms for known or suspected ethical or legal violations, and establishes minimum standards of behaviour expected of all employees. All employees must complete annual training on the code of business conduct. A "speaking up" policy is also in place so that members of staff are able to raise any instances of unethical acts, malpractice or impropriety. An additional process is also available to all staff via an international, anonymous help line operated by an independent company.

In order to support the welfare of its employees, the Northern Powergrid Group provides an employee assistance service to its staff via an independent company that supports over 350 organisations in the UK. The programme is a confidential, self-referral counselling and information service to assist with personal or work-related problems that may be affecting health, wellbeing or performance and is available 24 hours a day, 365 days a year. The services available include health, wellbeing and family-care information, financial information and debt counselling, and legal guidance. Working in partnership with its occupational health provider, the Northern Powergrid Group is delivering a long-term strategic programme aimed at improving the health of its staff and, in that respect, the Northern Powergrid Group won the Chartered Institute of Personnel and Development's North of England Award for Health and Wellbeing for its commitment and delivery of an improved health and well-being programme.

Progress continued to be made during the Regulatory Year on the key priorities in the human resources and organisational development functions, including recruitment, employee engagement, and performance management and development. Throughout the Regulatory Year, the Company continued to set and uphold the promotion of high standards of probity among staff. In addition, the Company's organisational structure has been developed to control business units and to delegate authority and accountability, having regard to acceptable levels of risk.

As at 31 March 2016, the Company employed 1,074 staff (2015: 1,065) and the numbers of males and females in the following categories were:

	Male	Female
Directors	7	1
Senior Managers	32	12
Total Number of Employees	868	206

As noted in the paragraph on management structure, operational management of the Company's business and that of its affiliate, NPg Yorkshire, is undertaken by a single senior management team, which is reflected in the above analysis.

CORE PRINCIPLES (CONTINUED)

Environmental respect

The Company's approach to environmental compliance is governed by its environmental policy and the policy of Environmental RESPECT (Responsibility, Efficiency, Stewardship, Performance, Evaluation, Communication and Training) implemented by Berkshire Hathaway Energy. These policies and their subordinate operational control procedures and systems address compliance with legal and other key environmental requirements, pollution prevention and continual improvement, and also promote environmental awareness and best practice amongst the Company's staff and contractors.

The Company has operated a United Kingdom Accreditation Service scheme for environmental management since the late 1990s, certified to the environmental management systems standard ISO 14001: 2004. It is subject to regular six-monthly assessment visits and a three-yearly certificate renewal assessment by an accredited external certification body in order to retain that status.

The most recent visit was a surveillance assessment carried out by Lloyd's Register Quality Assurance in September 2015. The assessment report drew management attention to two minor non-conformances to be addressed by agreed proposed actions and also noted that continued improvements had been made to the environmental management system over the past three years. There were no major non-conformances noted and, after a rigorous three-day surveillance audit, continued certification was recommended and subsequently confirmed.

Procedures and processes were reviewed and developed to improve the effectiveness of the environmental management system and operational controls at depots have also significantly improved, which has supported the reduced number of minor non-conformances raised at recent surveillance visits. In the event that fluid leakages do occur, the Company has in place an emergency incident response support contract with a specialist service provider, under which 24-hour environmental incident assistance is provided, including contamination mitigation, remediation and incident-validation reporting.

Improvements in support of the Company's environmental policy objectives continued to focus on replacing selected fluid-filled cable sections with non-fluid polymeric equivalents, replacing oil-filled circuit breakers with vacuum and sulphur hexafluoride gas-filled units at outdoor substations to reduce the potential for oil leakage and using gas tracer technology to locate cable fluid leaks quicker, where it was practicable to do so. The Company also provided environmental awareness training for staff via an online system to avoid the need for travelling to central training locations. These improvements support the Company in delivering sustained environmental performance, which it measures on a calendar year basis, and, in the year ended 31 December 2015, only four incidents were reportable to the Environment Agency, which was significantly better than the target of 10. Oil spills and leaks from the Company's assets exceeded the target of 13,500 litres by 4% and SF₆ gas discharges from electrical plant exceeded the target of 23 kilogrammes by 14%.

Environmental performance for the first quarter of 2016 was encouraging with leakage rates continuing to be below historic levels over that part of the year and was supported by increased awareness of environmental matters across the Company's business and effective and early notification of issues occurring that provide the opportunity to take action to manage those issues in a timely manner.

During the Regulatory Year, the Company recycled more of its waste than before and maintained its positive performance with regard to street works. Work continued with many of the Company's key stakeholders, including the Environment Agency, to enhance the advanced environmental management processes already in place and, in 2016, the Company plans to maintain this progress so that the impact on the environment in which it works is reduced and the most effective ways of doing so are utilised. The Company's business plan contains a commitment to reduce its business carbon footprint by 10% by the end of ED1 and performance remains on course to achieve that target.

CORE PRINCIPLES (CONTINUED)

Environmental respect (continued)

The Company's commitment to the Environmental RESPECT policy and its improved overall performance contributes towards minimising its impact on the environment. As part of its annual environmental improvement plan, the Company has mobilised significant programmes to replace fluid-filled cables and place overhead lines underground in National Parks and Areas of Outstanding Natural Beauty, reduce electrical losses and implement further improvements to the network that take account of protected structures, features, areas, wildlife and habitat. Bird life is being protected by placing bird-diverters on power lines where they are in proximity to nature reserves, wetlands, flight paths or in locations where rare species of bird are known to live or breed and also in response to information obtained from incident trends. During the Regulatory Year, the Company also initiated a pilot project with a not-for-profit social enterprise, which rescues waste timber and then provides affordable reclaimed timber products to the local community.

Sustainability

The Company's activities have an important part to play in the United Kingdom's transition to a low-carbon economy, both in its capacity as a major participant in the United Kingdom energy industry and in terms of its own carbon footprint.

As the country takes action to make significant reductions in its carbon emissions, the way electricity is produced and used is expected to have a significant impact on the electricity network over time. For example, the number of installations by customers of low-carbon technologies such as photovoltaic solar panels, electric vehicles and heat pumps continued to increase during the Regulatory Year and are reported via the regulatory reporting process. The volume and total capacity of decentralised energy generation has also been growing steadily for the last few years and, given the greater range of load and generation technologies now being connected to the network, the Company is taking action to develop innovative solutions that will reduce the need for traditional and potentially expensive reinforcement of the network.

In that respect, the Company disseminated the learning from its Customer-Led Network Revolution project during 2015, which was aimed at understanding how novel network technology and changes in customers' energy-usage habits may lead to the speedier and lower cost connection of low-carbon technologies to the network. The Company believes that the project delivered significant learning and a comprehensive legacy, as it developed practical guidance as well as policy recommendations and equipment specifications, made recommendations to update the United Kingdom electricity industry's technical network planning standards and delivered insight into potential future commercial arrangements and the practicalities of delivering end-solutions that are compatible with customers' needs.

The Company progressed new innovation projects during the Regulatory Year with a view to continuing to generate new knowledge and planned for the introduction of other new projects including the roll-out of enabling technology, reinforcement of the network to alleviate the constraints associated with low-carbon technologies and to support the roll-out of smart meters. By implementing its innovation strategy, the Company is investing in the facilitation of knowledge transfer and absorption of learning through the up-skilling of its workforce, the redefinition of its technical standards and the improvement of its processes. The Company is also actively involved in working with industry and other interested parties to develop national policies and strategies to assist the low-carbon transition. Consequently, the Company continues to believe that its plans will not only create some immediate benefits for customers during ED1, but also pave the way for much greater benefits after 2023.

The Company and its affiliate, NPg Yorkshire, measure and publish details of their business carbon footprints. Figures are reported per calendar year and relate solely to the regulated electricity distribution business. A monthly reporting process is in place to calculate the amount, based on an inventory of the various carbon emissions sources, identified with reference to the methodology described in the Greenhouse Gas Protocol and quantification of emissions is achieved through compilation of various operational data sources.

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STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

CORE PRINCIPLES (CONTINUED)

Environmental respect (continued)

Sustainability (continued)

The business carbon footprint associated with the Company's activities for the year ended 31 December 2015 was 22,014 tonnes carbon dioxide equivalent (2014: 22,746 tonnes), which includes work undertaken on the Company's behalf by its contractors but excludes electrical losses. The intensity ratio of emissions is measured as tonnes of greenhouse gas emissions per GWh distributed in the year and, for the Company, was 1.47 for the year ended 31 December 2015 a decrease of 3.2% compared to 2014, largely as a result of lower energy and fuel use recorded in the year. In line with Ofgem's requirements, the Company has contributed to the sustainability agenda through public reporting on its carbon footprint and its reporting framework is certified under CEMARS (the Certified Emissions Measurement and Reduction Scheme) for compliance with ISO 14064.

In July 2015, the Company submitted its second Adaptation to Climate Change report to the Department for Environment, Food and Rural Affairs, which builds on the actions identified in the first report and provides details of progress made against those actions. It also brings the report up to date to reflect the Northern Powergrid Group's structure and approach to risk management as well as discussing emerging research and its influence on the Northern Powergrid Group's approach to adaptation.

Updates from the first report include detail on the approach to surface water flooding, a review of industry practice for vegetation management and research carried out by Newcastle University into the effects of wind on electricity networks. The Company intends to continue to refine and adjust its plans and processes in the future, as more accurate climate projection data becomes available to take account of the potential impact that future climate change predictions may bring and to ensure that it continues to maintain the levels of network performance its customers deserve.

Regulatory integrity

The Company manages its business to the highest behavioural standards and adheres to a policy of strict compliance with all relevant standards, legislation and regulatory conditions. The Governance and Risk Management Group ("GRMG") is the principal risk management forum in the Northern Powergrid Group, and monitors and manages performance in risk-related and compliance areas. The GRMG met on three occasions during the Regulatory Year in order to review the mechanisms for meeting external obligations, to strengthen the business-control-improvement environment, and to consider and advise on key strategic risks facing the Company.

As has been the case for some years, breaches by a DNO of its licence conditions and certain other statutory requirements could lead to financial penalties, which Ofgem has stated "will have a proportionate impact on shareholder returns". In order to assure compliance with licence and other regulatory obligations, the Company operates a regulatory compliance affirmation process, under which ownership of approximately 1,750 regulatory obligations contained within the compliance database is currently assigned to around 75 responsible managers. Those responsible managers are required, on a quarterly basis, to review compliance with the relevant obligations that have been assigned to them for certification and report on any identified non-compliances or perceived risks to the compliance process, which are then addressed. The Regulation Manager reports to the board of directors on the outcome of each quarter's exercise.

Under the RIIO (revenue = incentives + innovation + outputs) model for regulation, price controls are set for eight years (rather than five as has previously been the case), with provision for a mid-period review of the outputs that network companies are required to deliver. The ED1 price control became effective on 1 April 2015 and is due to end on 31 March 2023.

STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

CORE PRINCIPLES (CONTINUED)

Regulatory integrity (continued)

The final determination in respect of ED1, as amended by the CMA, sets out the Company's allowed revenues and rules by which Ofgem expects to adjust these revenues in certain circumstances during ED1. Relative to Ofgem's original proposals, the CMA's determination resulted in the Company's base allowed revenue decreasing by approximately 0.1% in the regulatory year ended 31 March 2017 and in all subsequent years within ED1, before the addition of inflation (as measured by the Retail Prices Index ("RPI")). Base allowed revenue in the regulatory year ended 31 March 2016 remains unchanged from Ofgem's original final determination and nominal base allowed revenues will increase in line with RPI.

The ED1 price control is the first to be set for electricity distribution in Great Britain since Ofgem completed its review of network regulation (known as the RPI-X @ 20 project). The key changes to the price control calculations, compared to those used in previous price controls are that:

- the period over which new regulatory assets are depreciated is being gradually lengthened, from 20 years to 45 years, with the change being phased over eight years;
- allowed revenues will be adjusted during the price control period, rather than at the next price control review, to partially reflect cost variances relative to cost allowances;
- the allowed cost of debt will be updated within the price control period by reference to a long-run trailing average based on external benchmarks of public debt costs;
- allowed revenues will be adjusted in relation to some new service standard incentives, principally relating to speed and service standards for new connections to the network; and
- there is scope for a mid-period review and adjustment to revenues in the latter half of the period for any changes in the outputs required of licensees for certain specified reasons.

Many other aspects of the previous price control remain in place (either in their previous or similar form), including adjustments to revenues in relation to the number and duration of service interruptions and customer service standards. In addition, network tariffs, from which actual revenues are derived, are now set further in advance than was previously the case.

Changes have also been made to the legislation that prescribes the standards of service to be provided by the DNOs in specified circumstances and payments to be made to end-customers for failure to meet those standards. The most significant of these changes reduced from 18 to 12 hours the time that is allowed for restoration of supplies following an unplanned power cut in normal weather conditions.

With effect from 1 April 2015, the more formalised arrangements for assuring the accuracy of the information returns submitted to Ofgem, which had been trialled by network operators in the latter part of the previous price control period, entered into formal operation under the terms of the Licence. These arrangements involve the preparation and submission to Ofgem of a risk-based data-assurance plan for the regulatory year ahead, together with a report detailing the assurance work actually carried out in the regulatory year just ended and the findings of that work.

PRINCIPAL RISKS AND UNCERTAINTIES

There are a number of potential risks and uncertainties, which could have an impact on the Company, its financial position and its operations and may cause actual results to vary materially from those expected or historically experienced. The principal risks are outlined as follows:

Financial risk

As a holder of an electricity distribution licence, the Company is subject to regulation by GEMA, which acts through Ofgem. Most of the revenue of the electricity distribution licence holders is controlled by the distribution price control formula set out in the electricity distribution licence.

STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

PRINCIPAL RISKS AND UNCERTAINTIES (CONTINUED)

Financial risk (continued)

The price control formula does not constrain profits from year to year but sets the maximum permitted revenue for each regulatory year, taking into account base allowed revenues and movements in RPI, as well as factors such as performance against certain regulatory incentives. Where the Company recovers more, or less, than this maximum the difference is carried forward, with interest. For amounts relating to the regulatory year ended 31 March 2016, the carry forward will be into the entitlement for the regulatory year ended 31 March 2018.

The price control for ED1 has been set for the eight-year period commencing on 1 April 2015, although the price control formula may be reviewed at other times at the discretion of Ofgem, and it is Ofgem's intention to use eight-year price control periods in the future. A resetting of the formula is now made by GEMA without the consent of the electricity distribution licence holder, but a licensee can appeal to the CMA against a decision by GEMA to proceed with such a modification. Certain other interested parties have the same right. Details of the Company's appeal to the CMA can be found on page 3 of this Strategic Report.

During the term of the price control, the rate of inflation as measured by RPI is taken into account in setting the Company's allowed income in respect of each regulatory year. Consequently, one of the risks faced by the Company is that its costs may increase by more than RPI. Any changes in costs incurred will have a direct impact on the Company's financial results, as will changes in performance under incentive schemes, such as in customer service, which can lead to adjustments to allowed revenues.

Ofgem recognises that defined benefit pension schemes and, particularly, the current deficit positions of various schemes, represent a significant cost to the DNOs and, in its final proposals in respect of the previous price control period ("DPCR5"), Ofgem confirmed that DNOs would be allowed to recover the actuarial value of the deficits attributable to a licensee's distribution business in existence as at 31 March 2010 via its regulated revenues (after an adjustment to reflect the residual of unfunded early retirement deficiency costs as at 31 March 2010). Ofgem re-affirmed these principles in its ED1 final determination.

However, given the stable and regulated nature of the DNOs' businesses, Ofgem took the view that a notional repair period of 15 years from 1 April 2010 was appropriate for the purpose of assessing the DNOs' allowed revenues in respect of pension costs. Moreover, Ofgem reviews the reasonableness of the triennial actuarial valuations of DNOs' pension schemes and calculates new deficit funding allowances, including any adjustments that may be necessary to account for differences between allowances received and payments actually made to the relevant pension scheme.

The other financial risks facing the Company are outlined on pages 5 and 6 of this Strategic Report.

Operational risk

There are a number of risks to the Company's operational performance in respect of which mitigating actions have been taken. Appropriate credit cover arrangements are in place with the electricity suppliers, which would allow recovery of defaulted payments through the price control mechanism and a robust major incident management plan is implemented whenever severe weather impacts on the distribution network's performance. Given the regular instances of metal theft experienced in previous years, the Company maintained its programme of risk-assessed and enhanced security measures at its sites and pursued awareness raising activity at a national and local level, including commencing a social media campaign in early 2016 in partnership with Crimestoppers.

The Company recognises that there are uncertainties around the future take-up of low-carbon technologies and the resulting capacity requirements for the network, and from the fitting of smart meters throughout the Company's distribution services area, which is expected to result in a requirement to address a proportionate number of reported defects. The Company believes that it can effectively manage these issues through its usual risk management practices.

STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

PRINCIPAL RISKS AND UNCERTAINTIES (CONTINUED)

Commercial risk

Managing commercial risk continued to be of key importance and the Company remained focused on ensuring that its policies for credit checking, payment terms, payment performance tracking and debt management were strictly adhered to.

The Company's relationship with its main customers is governed by a distribution connection and use of system agreement ("DCUSA"), which is in place with each of those customers. Those customers are the electricity suppliers who, under the terms of the DCUSA, pay charges for the use of the distribution network, in respect of which it is necessary to ensure that credit cover arrangements in line with Ofgem's guidance remain in place. The principal electricity suppliers that use the Company's network are RWE Npower, British Gas, EDF Energy, E.ON, Scottish and Southern Energy and Scottish Power.

The Company operates utilising a mix of direct labour and contracted resource and has a range of contracts in place with various service providers for delivery of its work programmes, which are subject to regular market testing and tendering exercises. Those services include vegetation management, overhead line inspection and construction, substation construction and maintenance, underground cable laying services, vehicle leasing and servicing, tower refurbishment and information technology services. The Company also has an extensive suite of contracts in place for the procurement of all of the goods and equipment it requires to deliver its capital expenditure programme and to run its business, including for varying types of transformers, switchgear and cables

Risk Management

The Northern Powergrid Group operates a structured and disciplined approach to the management of risk as part of its overall risk management policy and, in DPCR5 and previous price control periods, accepted and successfully managed substantial cost and delivery risks by developing a culture of cost and risk management over that period of time. Risks are divided into a number of risk sectors which, in turn, align to the Northern Powergrid Group's Core Principles, as detailed on page 2 of this Strategic Report. A report regarding the effectiveness of each risk sector in terms of risk management, control activity, key success factors and supporting measures is presented at meetings of the GRMG. The risk environment is reviewed continually in order that new or emerging potential risks are identified.

The Northern Powergrid Group identifies and assesses risks associated with the achievement of its strategic objectives so that any actions needed to further enhance the control environment are identified, along with the person responsible for the management of the specific risk. A regular review of the key risks, controls and action plans is undertaken. The risk management programme includes regular review of the crisis management, disaster recovery and major incident plans, which are periodically tested, the sharing of best practice on disaster preparedness and response, disaster recovery tests of IT servers and priority processes, penetration tests against firewall systems, and a peer review of the Northern Powergrid Group's risk management systems by Berkshire Hathaway Energy.

Risk management continues to be a central theme of senior management priority setting, as well as an explicit business process that helps to identify lower probability, high consequence threats to business success or continuity. This approach is reinforced by that of the Berkshire Hathaway Energy group, whose activities have continued to include benchmarking of risk management activities across its business units, including the sharing of significant lessons learned associated with risk management.

A key element and requirement of the risk management process is that a written certificate is provided by the President and Chief Executive Officer of the Northern Powergrid Group confirming that the effectiveness of the system of internal controls has been reviewed during the year. A self-certification process is in place, in support of this review, whereby certain senior managers are required to confirm that the system of internal control in their area of the business is operating effectively. Consequently, the directors believe that a robust system of risk assessment and management is in place.

STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

PRINCIPAL RISKS AND UNCERTAINTIES (CONTINUED)

Internal Control

A rigorous internal control environment exists within the Northern Powergrid Group based on regular reporting, a series of operational and financial policy statements, investigations undertaken by internal audit and a stringent process for ensuring the implementation of any recommendations. Berkshire Hathaway Energy requires a quarterly risk control assessment to be undertaken by certain senior managers as part of its programme for compliance with the requirements of the United States Sarbanes-Oxley Act and, while no significant areas of weakness have been identified, any recommended improvements are implemented.

In addition, the Northern Powergrid Group employs comprehensive business planning and financial reporting procedures, regularly reviews key performance indicators to assess progress towards its goals and has a strong internal audit function to provide independent scrutiny of its internal control systems. The Northern Powergrid Group has risk management procedures in place, including the standards required by the United States Sarbanes-Oxley Act, and has centralised treasury operations and established procedures for the planning, approving and monitoring of major capital expenditure.

The Northern Powergrid Group is committed to maintaining the highest ethical standards in the conduct of its business and, in that respect, implements Berkshire Hathaway Energy's code of business conduct for employees. The code of conduct sets out and emphasises the required standards and commitment to ethical behaviour, provides reporting mechanisms for known or suspected ethical issues, helps prevent wrongdoing, and creates and sustains an ethical work environment across the Northern Powergrid Group. All employees are required to complete annual training on the code of business conduct and then confirm that they understand the requirements outlined in the code. The training is available online and employees who do not have access to the online system attend a briefing with their line manager.

The Company does not have a specific human rights policy but, as noted in this Strategic Report, it bases its operations on the Core Principles in order to deliver its long-term objectives. Accordingly, the Company remains fully committed to operating ethically and responsibly and with fairness and integrity through the policies and procedures it has in place which set the approach to its employees, their health, safety and welfare, its dealings with customers, particularly those who are vulnerable and on the priority services register, its impact on the environment and its contribution to the sustainability agenda within the energy industry. The Core Principles are a key factor in the responsible way in which the Company operates its electricity distribution business, examples of which are described throughout this Strategic Report.

The Northern Powergrid Group is also committed to preventing corruption in all its forms and continues to have a zero-tolerance approach to corruption in its business or by those with whom it does business. The board of Northern Powergrid Holdings Company has addressed the risks introduced by the Bribery Act 2010 through a compliance policy, changes to contractual terms, training and other staff awareness measures. The introduction of annual risk assessments and enhanced due diligence in respect of new business transactions has further assisted in ensuring compliance.

The Northern Powergrid Group requires staff, suppliers of services and business partners to comply with the Bribery Act. Its policies encourage an employee who has any suspicion of bribery or other form of corruption within or related to the Northern Powergrid Group to report the suspicion to a manager or via the international, anonymous help line mentioned in the Employee commitment section.

The Company has appropriate controls in place directed at ensuring compliance with the conditions in its Licence requiring any payments made to, or received from, affiliates or related undertakings in respect of goods and services provided or supplied to be on an arm's length basis and on normal commercial terms.

STRATEGIC REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

PRINCIPAL RISKS AND UNCERTAINTIES (CONTINUED)

Internal Control (continued)

In preparing these Regulatory Accounts, the directors have assessed the viability of the Company for the purposes of making the statement below and do so on an ongoing basis as part of the preparation and approval of the Company's ten-year business plan.

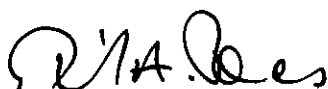
The directors have chosen the eight-year period from 1 April 2015 for the purposes of making this statement because it equates to the ED1 regulatory period, though longer periods may be appropriate given the 45-year life ascribed to the Company's new assets, the enduring nature of the Company's business and the fact that the notice period for revocation of the Company's electricity distribution licence is 25 years. The Company's income has been set for the ED1 regulatory period, although there is scope for a mid-period review and Ofgem may adjust revenues in the latter half of the period for any changes in the outputs required of the Company for certain specified reasons. Consequently and given the general stability associated with the regulatory environment in which the Company operates, the directors have been able to prepare sufficiently robust forecasts as part of the Company's annual business planning process, taking account of the principal risks and uncertainties which might have an impact on those forecasts. The Company's forecasts look forward for a 10-year period and anticipate the Company's continued stable operations beyond the ED1 price control.

Details of the principal risks and uncertainties, which could have an impact on the Company, are provided on pages 18 to 20 of the Strategic Report and details of how those principal risks are assessed and managed are provided in the Risk Management section of the Strategic Report.

The directors' ongoing assessment of the principal risks and uncertainties facing the Company also includes meeting the obligations in the Company's Licence to provide Ofgem with annual certificates, approved by the board, confirming that the directors have a reasonable expectation that the Company will have sufficient financial resources, financial facilities and operational resources available to it so that the Company is able to carry on its Distribution Business for a period of 12 months from the dates of those certificates. Assumptions taken into account when approving those certificates include (i) the potential for significant adverse financial impact from the various incentive schemes that can lead to variations in the Company's allowed income under its price control arrangements; (ii) the occurrence of catastrophic natural or other events, which could have a significant impact on the operating performance of the distribution network or involve significant expenditure; (iii) whether significant customer payment defaults may be experienced; and (iv) the continued availability to the Company of suitably qualified and experienced staff. Given the regulatory environment in which the Company operates, it is currently considered unlikely that there will be material variances to the assumptions used in providing those certificates during ED1.

The stable nature of the Company's business is evidenced by the fact that the commitments made by the Company in its well-justified business plan, which was originally submitted to Ofgem as part of the ED1 price control review process, have not changed fundamentally. Consequently, assuming that the principal risks and uncertainties facing the Company continue to be managed effectively, the directors have a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the ED1 period.

ON BEHALF OF THE BOARD:



P A Jones
Director

14 July 2016

NORTHERN POWERGRID (NORTHEAST) LIMITED

REGISTERED NUMBER 02906593

DIRECTORS' REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016

DIVIDENDS

During the Regulatory Year, an interim dividend of £20.6 million (10.3p per ordinary share) was paid (2014: £30.0 million, 15p per ordinary share). The directors recommended that no final dividend be paid in respect of the statutory accounting year ended 31 December 2015. No interim dividend was paid during the period from 1 January 2016 to 31 March 2016.

RESEARCH AND DEVELOPMENT

The Company supports a programme of research that is expected to contribute to higher standards of performance and a more cost-effective operation of its business. Having completed its major project under Ofgem's Low Carbon Networks Fund, known as the Customer-Led Network Revolution, the Company issued the draft project findings to Ofgem for consideration and then disseminated those findings more widely during 2015 as part of a three-month consultation period with the other DNOs in order to explore and refine the conclusions. The Company incurred expenditure of £31.0 million over the life of the project. Of that expenditure, 90% has been funded by electricity customers in Great Britain and Ofgem agreed that the Company was able to recover £2.7 million of the additional 10% from customers. The Company has the opportunity to apply in the future for a further discretionary award and Ofgem will consider additional rewards for those projects providing the best outcomes for customers. Further details of the Customer-Led Network Revolution project are provided in the Sustainability section on page 16 of the Strategic Report. New activities initiated in the Regulatory Year included projects regarding enhanced load reduction opportunities from customer participation, the accessing of disbursed domestic demand-side response and, alongside other utilities, how to determine optimum energy system technology approaches appropriate to local socio-economic factors. Other new activities during the Regulatory Year included alternative technology options for overhead line support and the use of unmanned aerial vehicles for remote asset inspection and management. Work completed during the year included the development of an improved decision support tool for optimum selection amongst complex asset investment options.

During the Regulatory Year, the Company invested £3.2 million (2015: £5.1 million) (Note 6 to the accounts) in its research and development activities.

FUTURE DEVELOPMENTS

The financial position of the Company, as at 31 March 2016, is shown in the statement of financial position on page 37.

There have been no significant events since the Regulatory Year end and the directors intend that the Company will continue to implement its well-justified business plan that was revised as part of the ED1 price control review process and will develop its business by operating with the goal of efficiently investing in the network and improving the quality of supply and service provided to customers.

DIRECTORS

The directors shown below have held office during the whole of the period from 1 April 2015 to the date of this report.

R Dixon	Non-executive Director
T E Fielden	Finance Director
J M France	Regulation Director
N M Gill	Operations Director
P A Jones	President and Chief Executive Officer
A J Maclennan	Business Development Director (appointed 17 July 2015)
A R Marshall	Non-executive Director
P C Taylor	Non-executive Director

J P Barnett resigned as a director with effect from 13 August 2015.

NORTHERN POWERGRID (NORTHEAST) LIMITED

REGISTERED NUMBER 02906593

DIRECTORS' REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

DIRECTORS (continued)

During and as at the end of the Regulatory Year, none of the directors was interested in any contract, which was significant in relation to the business of the Company.

During the Regulatory Year and up to the date of approval of the Directors' Report, an indemnity contained in the Company's Articles of Association was in force for the benefit of the directors of the Company and as directors of associated companies, which was a qualifying indemnity provision for the purposes of the Companies Act 2006.

FINANCIAL RISK MANAGEMENT

The Company's short-term financial objective is to ensure that it has access to sufficient liquidity to enable it to meet its obligations as they fall due and to provide adequately for contingencies. The long-term objective is to provide a stable and low cost of financing over time whilst observing approved risk parameters. The main risks are liquidity and interest rate risk.

Trading risk

Throughout the Regulatory Year, the Company's policy was that no trading in financial instruments should be undertaken.

Financial derivatives

As at 31 March 2016 and during the Regulatory Year it was the Company's policy not to hold any derivative financial instruments.

Further details of the financial risks facing the Company are provided in the Financial strength and Principal Risks and Uncertainties sections on pages 5 and 6 and 18 and 19 respectively of the Strategic Report.

POLITICAL DONATIONS

No contributions were made to political organisations during the Regulatory Year (2015: £nil).

EMPLOYEES

Employee consultation

The Company has a constitutional framework in place for employee consultation and has agreed that framework with trade union representatives. In addition, the Company communicates directly and through the management structure with non-collectively bargained staff, who are primarily of management grade, and keeps them informed of and involved as appropriate in developments that may impact on them now or in the future.

The Company is committed to maintaining and improving effective engagement and communication with employees. Following an employee engagement survey undertaken in 2014, senior and local engagement champions were identified during the Regulatory Year to work collaboratively with their teams in order to deliver agreed improvement plans. This approach is augmented by routine communication channels including regular staff briefs on current issues, meetings with staff and their representatives, and increased use of the Northern Powergrid Group's intranet to improve communication and engagement with the workforce.

During the Regulatory Year, the President and Chief Executive Officer of the Northern Powergrid Group continued to provide employees with updates on the Northern Powergrid Group's financial, organisational, safety and customer service performance through postings and weekly blogs on the Northern Powergrid Group's intranet on key elements of performance during the preceding week.

DIRECTORS' REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

EMPLOYEES (CONTINUED)

Disabled employees

The Company is committed to equality at work and, as such, its policy is to provide all protected groups, including disabled people, with equality at work in respect of employment, training, career development and promotion, having regard to their aptitudes and abilities. Should any member of staff become disabled during their employment, the Company would work to make reasonable adjustments, wherever possible.

Corporate Governance Statement

Although the Company does not have securities listed on the main market of the London Stock Exchange, the following statement is provided pursuant to paragraph 44.7 of standard condition 44 of the Licence, which requires the Company's Regulatory Accounts to include a Corporate Governance Statement, which has the coverage and content of such a statement that a Quoted Company is required to prepare. The Company provides the following statement setting out how it has applied the main principles in the version of the UK Corporate Governance Code made available on the Financial Reporting Council's website in September 2014 (the "Code"). To the extent that it departs from the Code, the Company explains from which parts of the Code it departs and the reasons for so doing.

Compliance statement

Set out below and in the Strategic Report are the areas in which the Company adopts and complies with the main principles of the Code. The Company has not complied with certain of the main principles of the Code, including main principles A2, A3, B2, B6, B7, D1, D2 and E2. The directors confirm that such non-compliance was of a continuing nature throughout the Regulatory Year but consider the governance framework in place to be appropriate to the circumstances of the Company, given that the framework is agreed with Berkshire Hathaway Energy and includes regular reporting to and meetings with the Chairman and senior management of Berkshire Hathaway Energy, the presence of independent, non-executive directors at board meetings of the Company and a strong internal control environment designed to meet the standards required by the United States Sarbanes-Oxley Act.

The Code is based on the "comply or explain" approach and the directors are of the opinion that, in the instances noted above where the Company does not comply with the Code, this approach is justifiable, given that the Company is a wholly-owned subsidiary of Berkshire Hathaway Energy and the governance framework in place throughout the Northern Powergrid Group is agreed with Berkshire Hathaway Energy.

Section A: Leadership

Main Principle A1: The Role of the Board

The directors have agreed a quarterly schedule of board meetings at which they review performance, strategy and operational and risk-related issues. Regular items on the agenda for consideration at board meetings include general business performance, regulatory compliance, operational issues and key business activities.

In addition, the President and Chief Executive Officer participates in weekly performance review meetings with the Chairman of Berkshire Hathaway Energy and other senior managers of the Berkshire Hathaway Energy group, including the Executive Vice President and Chief Financial Officer. At those weekly meetings, the views of the Chairman of Berkshire Hathaway Energy and the senior management team regarding the key, current issues facing the Northern Powergrid Group are discussed.

The Chairman of Berkshire Hathaway Energy also receives weekly, monthly, quarterly and ad-hoc reports on the Northern Powergrid Group's performance from the President and Chief Executive Officer. Berkshire Hathaway Energy's Executive Vice President and Chief Financial Officer and Senior Vice President and General Counsel also hold similar weekly review meetings in respect of Berkshire Hathaway Energy's financial and legal functions, at which the Northern Powergrid Group's Finance Director and General Counsel present their respective weekly reports.

NORTHERN POWERGRID (NORTHEAST) LIMITED

REGISTERED NUMBER 02906593

DIRECTORS' REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

Corporate Governance Statement (continued)

Section A: Leadership (continued)

Main Principle A1: The Role of the Board (continued)

The board meets quarterly and as required to consider relevant issues and met on six occasions during the Regulatory Year, with the attendance of the directors being as follows:

R Dixon	Non-Executive Director	5
T E Fielden	Finance Director	6
J M France	Regulation Director	5
N M Gill	Operations Director	5
P A Jones	President and Chief Executive Officer	4
A J MacLennan	Business Development Director	4 (of 4 following appointment)
A R Marshall	Non-Executive Director	6
P C Taylor	Non-Executive Director	4

Operational management of the Company's business (and that of its affiliate, NPg Yorkshire) is delegated to a single senior management team, with specific functional responsibilities. That senior management team meets monthly with the senior management of the Northern Powergrid Group to monitor performance and address issues of policy across all areas of the business and holds weekly conference calls to report on and consider performance-related issues for that week. Further details of the management structure of the Northern Powergrid Group are provided in the Strategic Report.

The directors have overall responsibility for the internal control environment, which, within the Northern Powergrid Group, is based on regular reporting, a series of operational and financial policy statements, investigations undertaken by internal audit and a stringent process for ensuring the implementation of any recommendations. In addition, Berkshire Hathaway Energy requires a quarterly risk control assessment to be undertaken by certain senior managers as part of its programme for compliance with the requirements of the United States Sarbanes-Oxley Act. The assessments undertaken during the Regulatory Year did not identify any significant weaknesses in the process but resulted in the implementation of recommended improvements. The key features of the Company's internal control system and the issues addressed by the Company during the Regulatory Year can be found in the Strategic Report.

A schedule of key delegations of authority has been approved by the board, which delegates authority for decision-making to senior and other managers in respect of issues such as capital expenditure, procurement, contractual, human resource and payment matters and for the conduct of claims and litigation. That schedule reserves decision-making to the directors above certain financial limits.

During the Regulatory Year, there were a number of committees in operation, acting under delegated terms of reference, which oversee Northern Powergrid Group and, therefore, Company policy. As part of their approved terms of reference, certain of those committees report regularly to the board on their activities.

The committees are as follows:

Health and Safety Management Committee

The board of Northern Powergrid Holdings Company has established the Northern Powergrid Group Health and Safety Management Committee with delegated powers to manage the health and safety policy and performance of the Northern Powergrid Group. The committee meets on a regular basis in order to oversee implementation of the health and safety policy, review and agree strategy for the management of health and safety issues, monitor health and safety performance across the Northern Powergrid Group, review the effectiveness of the health and safety policies and the health and safety management system, and consider recommendations for changes in policy due to changes in appropriate legislation, codes of practice or guidance or due to recommendations arising from investigations into significant incidents.

NORTHERN POWERGRID (NORTHEAST) LIMITED

REGISTERED NUMBER 02906593

DIRECTORS' REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

Corporate Governance Statement (continued)

Section A: Leadership (continued)

Main Principle A1: The Role of the Board (continued)

Health and Safety Management Committee (continued)

Membership of the committee comprises:

T E Fielden	Finance Director
J M France	Regulation Director
N M Gill	Operations Director
P A Jones	President and Chief Executive Officer
A J Maclellan	Business Development Director
G M Earl	Director of Health, Safety and Environment

Treasury Committee

The Treasury Committee oversees and implements the treasury policies, which are outlined in the Strategic Report and the Directors' Report, and comprises:

G E Abel	Chairman, Berkshire Hathaway Energy
L Bennett	Treasurer and Investor Reporting Manager
D Brady	Treasury and Reporting Manager
T E Fielden	Finance Director
P J Goodman	Executive Vice President and Chief Financial Officer, Berkshire Hathaway Energy
P A Jones	President and Chief Executive Officer
S J Lockwood	Group Financial Controller
S Gormally	Accounting Assistant and Secretary to the Committee

Pensions Committee

The Pensions Committee oversees the Northern Powergrid Group's approach to the pension schemes to which it contributes and comprises:

N Dawson	Senior Pensions Advisor
T E Fielden	Finance Director
J M France	Regulation Director
S J Lockwood	Group Financial Controller
K Mawson	Head of Regulatory Finance and Systems
L Tweedie	Head of Field Change
K Weatherburn	Director of Human Resources

Governance and Risk Management Group

The GRMG is the principal management forum in the Northern Powergrid Group with regard to corporate governance. Its purpose is to ensure that companies in the Northern Powergrid Group apply and maintain appropriate arrangements to deliver sound corporate governance and comply with the overall strategy, framework and supporting policies. The GRMG monitors and reviews the strategic risk environment, ensuring the continued suitability, adequacy and effectiveness of risk management arrangements and reports to the Northern Powergrid Group's Audit Committee.

NORTHERN POWERGRID (NORTHEAST) LIMITED

REGISTERED NUMBER 02906593

DIRECTORS' REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

Corporate Governance Statement (continued)

Section A: Leadership (continued)

Main Principle A1: The Role of the Board (continued)

Governance and Risk Management Group (continued)

The GRMG comprises:

N Applebee	Head of Shared Services
J Cardwell	Head of Trading and Innovation
R Dixon	Non-Executive Director
M Drye	Director of Asset Management
G M Earl	Director of Safety, Health and Environment
J Elliott	Company Secretary
T E Fielden	Finance Director
J M France	Regulation Director
T France	General Counsel
N M Gill	Operations Director
A Jones	Head of Strategic Planning and Delivery
A J Maclellan	Business Development Director
L Mackay	Head of Internal Audit
K Weatherburn	Director of Human Resources

Following implementation of a new process during Quarter 1 of 2015, which is designed to improve the effectiveness of the risk management and control activities, better define the risk environment within the Northern Powergrid Group, rationalise the reporting procedures to focus attention on key risk movements and identify accountabilities for each risk sector, the GRMG monitored the risk management framework regularly during the Regulatory Year to ensure that all strategic risks were being addressed. Risk management policies and procedures were reviewed and updated to ensure a robust and clear approach was maintained. Mr Dixon attended meetings of the GRMG to provide an independent view in respect of the matters discussed.

Asset risk continued to be a strong focus through the Asset Risk Management Executive Review Group and comprehensive plans continued to be in place to manage risks affecting all critical property assets and to strengthen the arrangements for crisis management and business continuity planning. In that respect, the Emergency Planning and Co-ordination Group (the "EPCG") has a remit to develop and maintain the Northern Powergrid Group's approach to emergency planning and to provide strategic leadership and guidance in respect of such matters.

The EPCG also ensures appropriate coordination between the various emergency planning disciplines, which include operational management of network incidents, property and the physical environment, non-operational management and resources and the support areas of human resources, information technology, health and safety, communications and legal services.

Further details of the Northern Powergrid Group's approach to corporate governance and the management of internal controls can be found in the Strategic Report.

As explained in respect of main principles B2 and D1, the Company does not have either a remuneration committee or a nomination committee.

Main Principle A2: Division of Responsibility

Mr G E Abel, the Chairman of Berkshire Hathaway Energy, is also Chairman of Northern Powergrid Holdings Company. As President and Chief Executive Officer, Dr Jones is responsible for the operation and management of both the Company and the Northern Powergrid Group and reports directly to Mr Abel.

DIRECTORS' REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

Corporate Governance Statement (continued)

Section A: Leadership (continued)

Main Principle A3: The Chairman

The board does not have a formally appointed Chairman. Dr Jones chairs board meetings, is responsible for the operation and management of both the Company and the Northern Powergrid Group and divides his time accordingly between his various commitments within the Northern Powergrid Group. Dr Jones reports directly to Mr Abel.

Main Principle A4: Non-Executive Directors

Three non-executive directors served on the board during the Regulatory Year, each of whom acts under the terms of their individual service contracts or terms of reference. Mrs A R Marshall and Professor P C Taylor were appointed to the board as non-executive directors in accordance with the requirement in condition 43A of the Company's Licence for the board to include two sufficiently independent directors, as defined in the Licence.

Section B: Effectiveness

Main Principle B1: The composition of the board

The board comprises five executive directors and three non-executive directors, who, collectively, bring a range of skills and experience to the board. Although the board does not include a balanced number of executive and non-executive directors, the board believes that it possesses the skills and experience necessary to provide effective leadership, stewardship and control of the Company, a position supported by the presence of the sufficiently independent directors required by the Company's licence.

Main Principle B2: Appointments to the board

The Company does not have a nomination committee. Appointments to the board are made by Berkshire Hathaway Energy, in conjunction with the President and Chief Executive Officer.

Main Principle B3: Commitment

The Company's non-executive directors commit sufficient time to preparation for and attendance at board meetings, although their service contracts or terms of reference do not quantify the time commitment required.

Main Principle B4: Development

The directors continually update their knowledge of and familiarity with the operations of the Company due to the robust reporting arrangements in place and have ongoing access to the Company's operations and its staff.

Main Principle B5: Information and support

Directors receive monthly reports outlining progress against the Company's goals and targets, enabling financial performance against budget and operational performance against a number of indicators to be reviewed, and also participate in weekly meetings, which consider the key issues of that week in some detail. The directors are able to utilise the advice and services of the Company Secretary, in respect of their duties and responsibilities as directors and any new legislation that may affect those duties and responsibilities. The directors also have access to external legal advice should they feel it necessary. Interim briefings are provided to the non-executive directors, as appropriate.

NORTHERN POWERGRID (NORTHEAST) LIMITED

REGISTERED NUMBER 02906593

DIRECTORS' REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

Corporate Governance Statement (continued)

Section B: Effectiveness (continued)

Main Principle B6: Evaluation

As part of their approved terms of reference, certain committees report regularly on their activities, enabling the directors to evaluate the activities of those committees. However, the board does not have a process of evaluation of its own performance or of the performance of individual directors in their capacity as directors. Berkshire Hathaway Energy has a performance appraisal and development scheme in place, under which each senior manager of the Northern Powergrid Group is subject to a formal annual appraisal of performance against his individual and Berkshire Hathaway Energy's goals.

Main Principle B7: Re-election

The Company's articles of association do not require periodic retirement and re-election of directors.

Section C: Accountability

Main Principle C1: Financial and business reporting

The board considers that the annual reports and accounts, which include the Strategic Report and the Report of the Directors, taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's performance, position, business model and strategy.

The directors explain, at page 2, the Core Principles behind the Company's strategy and, at page 33, their responsibility for preparing the Strategic Report, the Report of the Directors and the Regulatory Accounts, have reported, at page 32 in the Report of the Directors that the Company is a going concern and have included the Report of the Independent Auditor to the Company at pages 34 and 35 of these Regulatory Accounts.

Main Principle C2: Risk management and internal control

Details of the principal risks and uncertainties facing the Company and its internal control system, together with details of the issues addressed by the Company during the Regulatory Year, can be found at pages 18 to 22 of the Strategic Report. Also included at pages 23 and 24 of the Strategic Report is an explanation of how the prospects of the Company have been assessed, the period to which that assessment relates and the reasons as to why that period is considered to be appropriate.

Other key features of the internal control system are:

- Comprehensive business planning and financial reporting procedures, including the annual preparation of detailed operational budgets for the year ahead and projections for subsequent years;
- Regular review of key performance indicators to assess progress towards objectives;
- A range of policies, codes of practice and more detailed instructions that define the processes to be followed;
- A strong internal audit function, which provides independent scrutiny of internal control systems and risk management procedures, including the standards required by the United States Sarbanes-Oxley Act;

NORTHERN POWERGRID (NORTHEAST) LIMITED

REGISTERED NUMBER 02906593

DIRECTORS' REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

Corporate Governance Statement (continued)

Section C: Accountability (continued)

Main Principle C2: Risk management and internal control (continued)

- Ongoing health and safety performance reviews carried out by in-house safety professionals in addition to the regime of routine health and safety risk assessment and management processes carried out within each of the operating units;
- Processes and procedures to operate under OHSAS 18001, which is subject to external certification and regular assessment;
- An external obligations register, which assists with complying with financial, legal and regulatory obligations;
- Centralised treasury operations that operate within defined limits and are subject to regular reporting requirements and audit reviews; and
- Established procedures for planning, approving and monitoring major capital expenditure, major projects and the development of new business which includes short and long-term budgets, risk evaluation, detailed appraisal and review procedures, defined authority levels and post-investment performance reviews.

Main Principle C3: Audit committee and auditor

The board of Northern Powergrid Holdings Company has established an audit committee for the Northern Powergrid Group under delegated terms of reference, which include monitoring of the financial reporting process, the effectiveness of the internal control, internal audit and risk management systems, the statutory audit of the accounts, and the independence of and the provision of additional services by the auditor.

The Audit Committee comprises one member who is independent and one member who has competence in accounting, and receives annual reports from the GRMG and from the Northern Powergrid Group's Head of Internal Audit on the work of the Internal Audit Section during the year and the audit plan for the following year. The Audit Committee comprises:

R Dixon	Non-Executive Director
T E Fielden	Finance Director

Details of the fees paid by the Company to Deloitte LLP in relation to non-audit services during the Regulatory Year are provided in Note 6 to the accounts.

The employee section on page 14 of the Strategic Report contains details of the Company's "speaking up" policy.

Section D: Remuneration

Main Principle D1: The level and components of remuneration

The Company does not have a remuneration committee. Annual remuneration awards for the senior management of the Northern Powergrid Group are subject to the performance appraisal and development scheme process and consideration by the Chairman of Berkshire Hathaway Energy and the President and Chief Executive Officer. As the Company has no equity securities listed on the London Stock Exchange, it is not required to make directors' remuneration disclosures, other than those required for private companies.

DIRECTORS' REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

Corporate Governance Statement (continued)

Section D: Remuneration (continued)

Main Principle D2: Procedure

As noted under main principle D1, the Company does not have a remuneration committee. Annual remuneration awards for the senior management of the Northern Powergrid Group are subject to the performance appraisal and development scheme process and consideration by the Chairman of Berkshire Hathaway Energy and the President and Chief Executive Officer. No director is involved in deciding his own remuneration.

Section E: Relations with shareholders

Main Principle E1: Dialogue with Shareholders

As a wholly-owned subsidiary of a privately held group of companies, the board is in continuing dialogue with Berkshire Hathaway Energy.

Main Principle E2: Constructive use of General Meetings

This section of the Code is not applicable to the Company, as it is a wholly-owned subsidiary of a privately held group of companies and, therefore, has no institutional shareholders.

Going Concern

A review of the Company's business activities during the Regulatory Year, together with details regarding its future development, performance and position, its objectives, policies and processes for managing its capital, its financial risk management objectives and details of its exposures to trading risk, credit risk and liquidity risk are set out in the Strategic Report, the Report of the Directors and the appropriate notes to the Regulatory Accounts.

When considering continuing to adopt the going concern basis in preparing the Regulatory Accounts, the directors have taken into account a number of factors, including the following:

- The Company is a stable electricity distribution business operating an essential public service and is regulated by GEMA. In carrying out its functions, GEMA has a statutory duty under the Electricity Act 1989 to have regard to the need to secure that licence holders are able to finance the activities, which are the subject of obligations under Part 1 of the Electricity Act 1989 (including the obligations imposed by the electricity distribution licence) or by the Utilities Act 2000;
- The Company is profitable with strong underlying cash flows and holds investment grade credit ratings; and
- The Company is financed by long-term borrowings with an average maturity of 13 years and has access to borrowing facilities provided by Lloyds Bank plc, Royal Bank of Scotland plc and Abbey National Treasury Services plc.

Consequently, after making enquiries, the directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the Regulatory Accounts.

NORTHERN POWERGRID (NORTHEAST) LIMITED

REGISTERED NUMBER 02906593

DIRECTORS' REPORT FOR THE REGULATORY YEAR ENDED 31 MARCH 2016 (CONTINUED)

Responsibility statement of the Directors for the preparation of the Regulatory Accounts

The directors are responsible for preparing the Regulatory Accounts, including the Strategic Report, the Directors' Report and the Corporate Governance Statement in accordance with standard condition 44 of the Licence and in accordance with International Financial Reporting Standards ("IFRS"). These Regulatory Accounts have been prepared on a consistent basis with those for the year ended 31 March 2015.

In preparing financial statements, International Accounting Standard 1 requires the directors to:

- Properly select and apply accounting policies;
- Present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- Provide additional disclosures when compliance with the specific requirements in IFRS are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Company's financial position and financial performance; and
- Make an assessment of the Company's ability to continue as a going concern.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities. The directors are responsible for the maintenance and integrity of any corporate and financial information relating to the Company, which is included on the Northern Powergrid Group's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions

Audit of the accounts

Each of the directors, who is a director of the Company as at the date of this report, confirms that:

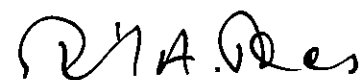
- a) so far as he or she is aware, there is no relevant audit information of which the Company's auditor is unaware; and
- b) he or she has taken all the steps he ought to have taken as a director in order to make him or herself aware of any relevant audit information and to establish that the auditor is aware of that information.

This confirmation should be interpreted in accordance with the provisions of section 418 of the Companies Act 2006.

Auditor

Deloitte LLP will continue in office in accordance with the provisions in section 487 of the Companies Act 2006 and has indicated its willingness to do so.

ON BEHALF OF THE BOARD:



P A Jones
Director

14 July 2016

INDEPENDENT AUDITOR'S REPORT TO THE GAS AND ELECTRICITY MARKETS AUTHORITY ("THE REGULATOR") AND NORTHERN POWERGRID (NORTHEAST) LIMITED ("THE COMPANY")

We have audited the Regulatory Accounts of the Company for the regulatory year ended 31 March 2016 (the "Regulatory Accounts") on pages 36 to 72 which comprise the Statement of Profit or Loss and Other Comprehensive Income, the Statement of Comprehensive Income, the Statement of Financial Position, the Statement of Changes in Equity, the Statement of Cash Flows and the related notes numbered 1 to 26. These Regulatory Accounts have been prepared under the accounting policies set out therein.

This report is made, on terms that have been agreed, solely to the Company and the Regulator in order to meet the requirements of Standard Condition 44 of the Electricity Distribution Licence, (the "Regulatory Licence"). Our audit work has been undertaken so that we might state to the Company and the Regulator those matters that we have agreed to state to them in our report, in order (a) to assist the Company to meet its obligation under the Regulatory Licence to procure such a report and (b) to facilitate the carrying out by the Regulator of its regulatory functions, 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 Regulator for our audit work, for this report or for the opinions we have formed.

Basis of preparation

The Regulatory Accounts have been prepared under the historical cost convention and in accordance with the Regulatory Licence and the accounting policies set out in the notes to the Regulatory Accounts.

The Regulatory Accounts are separate from the statutory financial statements of the Company (the "Statutory Accounts") and have not necessarily been prepared under the basis of International Financial Reporting Standards as endorsed by the European Union ("IFRS"). Financial information other than that prepared on the basis of IFRS does not necessarily represent a true and fair view of the financial performance or financial position of a company as shown in financial statements prepared in accordance with the Companies Act 2006.

Respective responsibilities of the Regulator, the Directors and auditor

The nature, form and content of the Regulatory Accounts are determined by the Regulator. It is not appropriate for us to assess whether the nature of the information being reported upon is suitable or appropriate for the Regulator's purposes. Accordingly we make no such assessment.

The Directors' responsibilities for preparing the Regulatory Accounts in accordance with Condition 44 of the Regulatory Licence are set out in the statement of directors' responsibilities on page 33.

Our responsibility is to audit the Regulatory Accounts in accordance with International Standards on Auditing (UK & Ireland) issued by the Auditing Practices Board, except as stated in the 'Basis of audit opinion', below and having regard to the guidance contained in Audit 05/03 *'Reporting to Regulators of Regulated Entities'*.

We report to you our opinion as to whether the Regulatory Accounts present fairly, in accordance with Standard Condition 44 of the Regulatory Licence and the accounting policies set out on pages 40 to 47, the results and financial position of the Company for the regulatory year ended 31 March 2016. We also report to you if, in our opinion, the Company has not kept proper accounting records or if we have not received all the information and explanations that we require for our audit.

We read the other information presented with the Regulatory Accounts, being the strategic report, the directors' report, the corporate governance statement and the statement of directors' responsibilities, on which we do not express an audit opinion, and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Regulatory Accounts.

**INDEPENDENT AUDITOR'S REPORT TO THE GAS AND ELECTRICITY MARKETS AUTHORITY
("THE REGULATOR") AND NORTHERN POWERGRID (NORTHEAST) LIMITED ("THE COMPANY")
(CONTINUED)**

Basis of opinion

We conducted our audit in accordance with International Standards on Auditing (UK & Ireland) issued by the UK Auditing Practices Board, except as noted below. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Regulatory Accounts. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the Regulatory Accounts and of whether the accounting policies are 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 Regulatory Accounts are free from material misstatement, whether caused by fraud or other irregularity or error. However, as the nature, form and content of the Regulatory Accounts are determined by the Regulator, we did not evaluate the overall adequacy of the presentation of the information, which would have been required if we were to express an audit opinion under United Kingdom Auditing Standards.

Our opinion on the Regulatory Accounts is separate from our opinion on the Statutory Accounts, on which we reported on 14 April 2016, which are prepared for a different purpose. Our audit report in relation to the Statutory Accounts (our "statutory audit") was made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our statutory audit was undertaken so that we might state to the Company's members those matters we are required to state to them in a statutory auditor's report and for no other purpose. In these circumstances, to the fullest extent permitted by law, we do not accept or assume any responsibility to anyone other than the Company and the Company's members as a body, for our statutory audit, for our statutory audit report, or for the opinions we have formed in respect of that statutory audit.

Audit opinion

In our opinion the Regulatory Accounts

- present fairly in accordance with Standard Condition 44 of the Regulatory Licence and the accounting policies set out on pages 40 to 47, the financial position of the Company as at 31 March 2016 and of its financial performance and cash flows for the year then ended; and
- have been properly prepared in accordance with Standard Condition 44 of the Regulatory Licence and the Company's accounting policies.

Deloitte CP

Deloitte LLP
Chartered Accountants and Registered Auditor
Newcastle upon Tyne

27 July 2016

STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 MARCH 2016

	Notes	2016 £m	2015 £m
Revenue	3	327.5	372.8
Cost of sales		<u>(12.4)</u>	<u>(24.2)</u>
Gross profit		315.1	348.6
Distribution costs		<u>(101.9)</u>	<u>(94.6)</u>
Administrative expenses		<u>(69.9)</u>	<u>(71.1)</u>
Operating profit	6	143.3	182.9
Profit on disposal of property, plant and equipment		0.5	0.7
Investment income	7	0.1	0.1
Finance costs	8	<u>(27.1)</u>	<u>(25.9)</u>
Profit before tax		116.8	157.8
Income tax expense	9	<u>(9.8)</u>	<u>(32.6)</u>
Profit on ordinary activities after taxation		107.0	125.2
Ordinary dividends on equity shares	10	<u>(20.6)</u>	<u>(30.0)</u>
Profit for the financial year		<u>86.4</u>	<u>95.2</u>

All activities relate to continuing operations.

STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 MARCH 2016

There has been no other comprehensive income for the Company. Therefore, total comprehensive income for the year is £107.0 million (2015: £125.2 million).

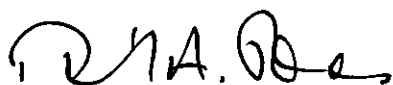
NORTHERN POWERGRID (NORTHEAST) LIMITED

REGISTERED NUMBER 02906593

STATEMENT OF FINANCIAL POSITION AS AT 31 MARCH 2016

	Notes	2016 £m	2015 £m
Assets			
Non-current assets			
Property, plant and equipment	11	2,147.6	2,028.9
Intangible assets	12	33.6	26.6
		<u>2,181.2</u>	<u>2,055.5</u>
Current assets			
Inventories	14	11.6	12.1
Trade and other receivables	15	54.7	58.0
		<u>66.3</u>	<u>70.1</u>
Total assets		<u>2,247.5</u>	<u>2,125.6</u>
Equity			
Called-up share capital	21	200.0	200.0
Retained earnings		643.2	556.8
Total equity		<u>843.2</u>	<u>756.8</u>
Liabilities			
Current liabilities			
Trade and other payables	16	94.8	105.8
Tax payable	16	4.5	13.5
Borrowings	17	67.7	153.0
Deferred revenue	19	20.1	21.3
Provisions	20	1.2	1.3
		<u>188.3</u>	<u>294.9</u>
Non-current liabilities			
Borrowings	17	586.9	466.8
Deferred tax	18	95.5	101.5
Deferred revenue	19	533.3	505.3
Provisions	20	0.3	0.3
		<u>1,216.0</u>	<u>1,073.9</u>
Total liabilities		<u>1,404.3</u>	<u>1,368.8</u>
Totally equity and liabilities		<u>2,247.5</u>	<u>2,125.6</u>

The financial statements were approved by the board of directors and authorised for issue on 14 July 2016 and were signed on its behalf by:



P A Jones
Director

NORTHERN POWERGRID (NORTHEAST) LIMITED

REGISTERED NUMBER 02906593

STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 MARCH 2016

	Share Capital	Retained Earnings	Total Equity
	£m	£m	£m
At 1 April 2014	200.0	461.6	661.6
Total comprehensive income for the year	-	125.2	125.2
Dividends paid	-	(30.0)	(30.0)
	<hr/>	<hr/>	<hr/>
At 1 April 2015	200.0	556.8	756.8
Total comprehensive income for the year	-	107.0	107.0
Dividends paid	-	(20.6)	(20.6)
	<hr/>	<hr/>	<hr/>
At 31 March 2016	200.0	643.2	843.2

NORTHERN POWERGRID (NORTHEAST) LIMITED**REGISTERED NUMBER 02906593****STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 MARCH 2016**

	Notes	2016 £m	2015 £m
Cash Flows from operating activities			
Cash generated from operations	22	196.8	219.1
Finance costs paid		(29.4)	(29.2)
Tax paid		(24.8)	(29.3)
Net cash from operating activities		<u>142.6</u>	<u>160.6</u>
Cash flows used in investing activities			
Purchase of property, plant and equipment		(204.6)	(205.6)
Purchase of intangible assets		(9.8)	(10.3)
Proceeds from disposals of property, plant and equipment		0.5	0.7
Receipt of customer contributions		<u>58.2</u>	<u>43.3</u>
Net cash used in investing activities		<u>(155.7)</u>	<u>(171.9)</u>
Cash flows from financing activities			
Equity dividends paid		(20.6)	(30.0)
Borrowings		46.6	31.8
Movement in loans from Group undertaking		<u>(12.9)</u>	<u>9.5</u>
Net cash from financing activities		<u>13.1</u>	<u>11.3</u>
Net movement in cash and cash equivalents		-	-
Cash and cash equivalents at beginning of year		-	-
Cash and cash equivalents at end of year		<u>-</u>	<u>-</u>

NORTHERN POWERGRID (NORTHEAST) LIMITED

REGISTERED NUMBER 02906593

NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016

1 GENERAL INFORMATION

Northern Powergrid (Northeast) Limited is a company incorporated in England and Wales and is part of the Northern Powergrid Holdings Company group of companies (the "Northern Powergrid Group"). The company is registered in England and Wales and the address of the registered office is Lloyds Court, 78 Grey Street, Newcastle-upon-Tyne, NE1 6AF.

The nature of the Company's business model, strategic objectives, operations and activities are set out in the Strategic Report and in the Directors' Report.

2 ACCOUNTING POLICIES

Accounting convention and basis of preparation

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). The financial statements have also been prepared in accordance with IFRS adopted by the European Union and therefore comply with Article 4 of the EU IAS Regulation and with those parts of the Companies Act 2006 (the "Act") that are applicable to companies reporting under IFRS.

The accounts have been prepared under the historical cost convention. The Company has relied upon Section 400 of the Act and has presented the accounts for the Company as an individual undertaking only and not as a Group undertaking.

Going Concern

The directors have, at the time of approving the financial statements, a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the financial statements. Further detail is contained within the Directors' Report on page 32.

Judgments in applying accounting policies and key sources of estimation uncertainty

Many of the amounts included in the financial statements involve the use of judgment and/or estimation. These judgments and estimates are based on management's best knowledge of the relevant facts and circumstances, having regard to previous experience but actual results may differ from the amounts included in the financial statements. Information about such judgments and estimates is contained in the accounting policies and/or the notes to the financial statements and the key areas are summarised below.

Areas of judgment and estimation which have the most significant effect on the amounts recognised in the financial statements are:

- The estimation of useful economic lives for property, plant and equipment;
- The split of operating and capital expenditure and the allocation of overheads to capital; and
- Impairment reviews carried out to evaluate the carrying value of assets held at the statement of financial position date.

Critical accounting policies

The critical accounting policies adopted by the directors relate to property, plant and equipment, taxation, pensions and revenue and are described below. The accounting policies have been applied consistently throughout the year and the preceding year.

NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

2 ACCOUNTING POLICIES (CONTINUED)

Adoption of new or revised standards

In the current year, the Company has applied a number of amendments to IFRS issued by the International Accounting Standards Board ("IASB") that are mandatorily effective for an accounting period that begins on or after 1 April 2015:

- Amendments to IAS 19 – Defined Benefit Plans: Employee Contributions. The amendments to IAS 19, Defined Benefit Plans: Employee Contributions, clarify how an entity should account for contributions made by employees or third parties to defined benefit plans, based on whether those contributions are dependent on the number of years of service provided by the employee. The application of these amendments to IAS 19 has not had an impact on the Company's financial statements.
- Annual Improvements to IFRS 2010-2012 Cycle and Annual Improvements to IFRS 2011-2013 Cycle. The Annual Improvements to IFRS 2010-2012 Cycle and IFRS 2011-2013 Cycle include a number of amendments to various IFRS. The application of these amendments has not had a significant impact on the Company's financial statements.

The Company has not applied the following new and revised IFRS that have been issued but are not yet effective for the year ended 31 March 2016:

- IFRS 9 - Financial Instruments (1 January 2018). A revised version of IFRS 9, Financial Instruments, was issued in July 2014 mainly to include: a) impairment requirements for financial assets; and b) limited amendments to the classification and measurement requirements by introducing a 'fair value through other comprehensive income' ("FVTOCI") measurement category for certain simple debt instruments. The directors of the Company anticipate that the application of IFRS 9 in the future is unlikely to have an impact on amounts reported in respect of the Company's financial assets and financial liabilities.

NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

2 ACCOUNTING POLICIES (CONTINUED)

Adoption of new or revised standards (continued)

- IFRS 15 - Revenue from Contracts with Customers (1 January 2018). In May 2014, IFRS 15, Revenue from Contracts with Customers, was issued which establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. IFRS 15 will supersede the current revenue recognition guidance including IAS 11 Construction Contracts, IAS 18 Revenue and the related Interpretations. The core principle of IFRS 15 is that an entity should recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Under IFRS 15, an entity recognises revenue when (or as) a performance obligation is satisfied. Far more prescriptive guidance has been added in IFRS 15 to deal with specific scenarios. Furthermore, extensive disclosures are required by IFRS 15. The directors anticipate that the application of IFRS 15 in the future may have a material impact on the amounts reported and disclosures made in the Company's financial statements. However it is not practicable to provide a reasonable estimate of the effect until the Company undertakes a detailed review.
- IAS 1 – Disclosure Initiative (1 January 2016). The amendments to IAS 1 give some guidance on how to apply the concept of materiality in practice. The directors do not anticipate that the application of these changes will have a material impact on the Company's financial statements.
- Amendments to IAS 16 and IAS 38 - Clarification of Acceptable Methods of Depreciation and Amortisation (1 January 2016). The amendments to IAS 16 and IAS 38, Clarification of Acceptable Methods of Depreciation and Amortisation, prohibit entities from using a revenue-based depreciation method for items of property, plant and equipment. The amendments to IAS 38 introduce a rebuttable presumption that revenue is not an appropriate basis for the amortisation of an intangible asset. Currently the Company uses the straight-line method for depreciation and amortisation of property, plant and equipment, and intangible assets. The directors believe that the straight-line method is the most appropriate method to reflect the consumption of economic benefits inherent in the respective assets and accordingly, the directors do not anticipate that the application of these amendments will have a material impact on the Company's financial statements.
- Annual Improvements to IFRS 2012-2014 Cycle. The Annual Improvements to IFRS 2012-2014 Cycle include a number of amendments to various IFRS. The directors do not anticipate that the application of these amendments will have a significant impact on the Company's financial statements.

NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

2 ACCOUNTING POLICIES (CONTINUED)

Adoption of new or revised standards (continued)

- IFRS 16 – Leases IFRS 16 will have an impact on accounting for leases as the Company holds operating lease commitments. However, it is estimated that this will not be significant.

Note: IFRS 14, Regulatory Deferral Accounts, is not applicable to the Company as the Company is not a first-time adopter of IFRS.

The directors are not aware of any other newly issued or modified Standards and Interpretations that are not yet effective which would have a material impact on these financial statements.

Revenue

Revenue is only recognised when the risks and rewards of ownership have been transferred to a third party. No revenue is recognised where there are significant uncertainties regarding the consideration to be received or the costs associated with the transaction.

Revenue represents charges for the use of the Company's distribution network, amortisation of customer contributions, rental of meters, recharge of costs incurred on behalf of related parties and the invoiced value of other goods sold and services provided, exclusive of value added tax.

Revenues from charges to end customers for the use of the Company's distribution network include estimates of the units distributed. The estimated usage is based on historic data, judgment and assumptions. Revenues are gradually adjusted to reflect actual usage in the period during which actual meter readings are obtained.

Any under or over-recovery of allowed distribution network revenues, as prescribed by Ofgem, is not provided for in the financial statements and will be recovered/repaid through future tariffs.

Customer contributions towards distribution system assets are included in deferred revenue. The Company's policy is to credit the customer contribution to revenue on a straight-line basis, in line with the useful life of the distribution system assets.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable.

Dividend income from investments is recognised when the shareholders' rights to receive payment have been established.

Research costs

Expenditure on research activities is written off to the statement of profit or loss in the year in which it is incurred.

Operating profit

Operating profit is stated before investment income, finance costs, profit on sale of property, plant and equipment and income from other fixed asset investment.

NORTHERN POWERGRID (NORTHEAST) LIMITED

REGISTERED NUMBER 02906593

NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

2 ACCOUNTING POLICIES (CONTINUED)

Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the statement of profit or loss because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted at the statement of financial position date.

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit and is accounted for using the statement of financial position liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each statement of financial position date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the year when the liability is settled or asset realised, based on tax rates and tax legislation enacted or substantively enacted at the statement of financial position date.

Property, plant and equipment and depreciation

Property, plant and equipment is stated at cost. Cost includes the purchase price of the asset and any costs, including internal employee and other costs, directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.

The charge for depreciation is calculated to write off assets to their residual values over their estimated useful lives using the straight-line basis:

Distribution system assets.....	45 years
Distributed generation assets included in distribution system assets.....	15 years
Metering equipment included in distribution system assets	up to 5 years
Information technology equipment included in distribution system assets.....	up to 10 years
Non-operational assets:	
Buildings – freehold.....	up to 60 years
Buildings – leasehold.....	lower of lease period or 60 years
Fixtures and equipment.....	up to 10 years
Software development costs	up to 10 years

Freehold land is not depreciated.

Assets in the course of construction are carried at cost. Depreciation on these assets, on the same basis as other assets, commences when the assets are commissioned.

NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

2 ACCOUNTING POLICIES (CONTINUED)

Property, plant and equipment and depreciation (continued)

The estimated useful economic lives of property, plant and equipment are based on management's judgment and experience. When management identifies that actual useful lives differ materially from the estimates used to calculate depreciation, that charge is adjusted prospectively. Due to the significance of the Company's investment in property, plant and equipment, variations between actual and estimated useful lives could impact operating results both positively and negatively, although historically few changes to estimated useful lives have been required.

The Company is required to evaluate the carrying values of property, plant and equipment for impairment whenever circumstances indicate, in management's judgment, that the carrying value of such assets may not be recoverable. An impairment review requires management to make judgments concerning the cash flows, growth rates and discount rates for the cash-generating units under review.

Software development costs

Costs in respect of major developments are capitalised and amortised over the expected life of the software. Capitalised software costs that are not an integral part of the related hardware are included in intangible assets on the statement of financial position and amortised on a straight line basis over the expected life of the software of up to 10 years.

Investments

Fixed asset investments are stated at cost less provision for impairment in value.

Inventories

Inventories are stated at the lower of cost and net realisable value as follows:

Raw materials and consumables are valued at purchase cost determined on an average price basis.

Work in progress is valued at the cost of direct materials and labour plus attributable overheads based on the normal level of activity less progress payments.

Net realisable value is based on estimated selling price less further costs expected to be incurred to completion and disposal.

Provisions

Provisions are recognised when the Company has a present obligation as a result of a past event and it is probable that the Company will be required to settle that obligation. Provisions are measured at the directors' best estimate of the expenditure required to settle the obligation at the statement of financial position date. Reasonable estimates involve judgments made by management after considering information including notifications, settlements, estimates performed by independent parties and legal counsel, available facts, identification of other potentially responsible parties and their ability to contribute and prior experience.

Where the effect is significant, provisions in respect of material future liabilities are stated at their net present value and arrived at by discounting the anticipated future costs at the market rate at the statement of financial position date.

NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

2 ACCOUNTING POLICIES (CONTINUED)

Leases

Leases are classified as finance leases wherever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Operating lease rentals are charged to the statement of profit or loss in equal annual amounts over the lease term.

Trade receivables

Trade receivables are measured at initial recognition at fair value. Appropriate allowances for estimated irrecoverable amounts are recognised in the statement of profit or loss when there is objective evidence that the asset is impaired.

Trade payables

Trade payables are not interest bearing and are stated at their nominal value.

Borrowings

Borrowings are classified as other financial liabilities at amortised cost. They are recorded at the proceeds received, net of direct issue costs. Finance charges, including premiums payable on settlement for redemption and direct issue costs, are accounted for on an accruals basis in the statement of profit or loss using the effective interest rate method. They are added to the carrying amount of the instruments to the extent that they are not settled in the period in which they arise. Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset are capitalised as part of the cost of that asset.

Financial instruments

Financial assets and financial liabilities are recognised on the statement of financial position when the Company becomes a party to the contractual provisions on the instrument.

Financial assets are assessed for indicators of impairment at each statement of financial position date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted.

For certain categories of financial assets, such as trade receivables, assets that are assessed not to be impaired individually are subsequently assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of receivables could include the Company's past experience of collecting payments, an increase in the number of delayed payments in the portfolio past the average credit period of 30 days, as well as observable changes in national or local economic conditions that correlate with default on receivables.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables, where the carrying amount is reduced through the use of an allowance account. When a trade receivable is considered uncollectable, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in the statement of profit or loss.

NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

2 ACCOUNTING POLICIES (CONTINUED)

Fair value measurements

For financial reporting purposes, fair value measurements are categorised into Level 1, 2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement in its entirety, which are described as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company can access at the measurement date;
- Level 2 inputs are inputs, other than quoted prices included within Level 1, that are observable for the asset or liability, either directly or indirectly; and
- Level 3 inputs are unobservable inputs for the asset or liability.

Financial liabilities and equity

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangement entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Company after deducting all of its liabilities.

Pensions

The Company contributes to the Northern Powergrid Group of the Electricity Supply Pension Scheme (the "Northern Powergrid Group of the ESPS"). The Northern Powergrid Group of the ESPS is a defined benefit plan that shares risk between various entities under common control. There is no contractual agreement or stated policy for charging the net defined benefit cost for the plan as a whole to individual group entities and accordingly the Company accounts for the Northern Powergrid Group of the ESPS as if it were a defined contribution scheme. Contributions to the Northern Powergrid Group of the ESPS are charged to the statement of profit or loss or capitalised as appropriate. The capital costs of ex-gratia and supplementary pensions are normally charged to the statement of profit or loss in the period in which they are granted. Accounting actuarial valuations are carried out at each financial year end with the last one being undertaken as at 31 December 2015. A separate valuation is not carried out at the regulatory reporting year end in accordance with a derogation to the Company's distribution licence.

The Company also participates in a defined contribution scheme. Contributions payable to the defined contribution scheme are charged to the statement of profit or loss in the year or capitalised as appropriate. Differences between contributions payable in the year and contributions actually paid are shown as either accruals or prepayments in the statement of financial position.

NORTHERN POWERGRID (NORTHEAST) LIMITED

REGISTERED NUMBER 02906593

NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

3 SEGMENTAL REPORTING

IFRS 8 requires operating segments to be identified on the basis of internal reports about components of the Company that are regularly reviewed by the President and Chief Executive Officer of the Northern Powergrid Group in order to allocate resources to those segments and to assess their performance.

In practice, the President and Chief Executive Officer allocates resources and assesses performance based upon the aggregate results of the Company and Northern Powergrid (Yorkshire) plc, another distribution network operator in the Northern Powergrid Group, suggesting that no segmental reporting is required. However, in accordance with the Company's distribution licence, the Company must publish certain segmental information in the Regulatory Accounts, as follows:

	Distribution 2016 £m	Distributed Generation 2016 £m	Excluded Services 2016 £m	Metering 2016 £m	De Minimis 2016 £m	Total 2016 £m
STATEMENT OF PROFIT OR LOSS						
Revenue	300.1	1.1	2.4	4.9	19.0	327.5
Cost of sales	(10.3)	-	(1.0)	-	(1.1)	(12.4)
Gross profit	289.8	1.1	1.4	4.9	17.9	315.1
Distribution costs	(96.2)	(4.2)	-	(1.5)	-	(101.9)
Administration costs	(51.2)	-	(0.5)	(0.6)	(17.6)	(69.9)
Operating profit/(loss)	142.3	(3.1)	0.9	2.8	0.3	143.3
OTHER INFORMATION						
Capital tangible additions	151.7	9.0	30.5	0.1	-	191.3
Capital intangible additions	9.1	0.2	0.5	-	-	9.8
	Distribution 2015 £m	Distributed Generation 2015 £m	Excluded Services 2015 £m	Metering 2015 £m	De Minimis 2015 £m	Total 2015 £m
STATEMENT OF PROFIT OR LOSS						
Revenue	344.4	2.5	2.2	5.1	18.6	372.8
Cost of sales	(21.9)	-	(0.8)	-	(1.5)	(24.2)
Gross profit	322.5	2.5	1.4	5.1	17.1	348.6
Distribution costs	(89.6)	(3.9)	-	(1.1)	-	(94.6)
Administration costs	(54.1)	-	(0.5)	(0.2)	(16.3)	(71.1)
Operating profit/(loss)	178.8	(1.4)	0.9	3.8	0.8	182.9
OTHER INFORMATION						
Capital tangible additions	192.0	5.5	25.2	0.6	-	223.3
Capital intangible additions	9.7	0.1	0.5	-	-	10.3

Revenue is all in respect of sales to United Kingdom customers.

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NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

4 STAFF COSTS

	2016 £m	2015 £m
Salaries	49.9	48.9
Social security costs	5.0	4.8
Defined benefit pension costs	28.2	32.2
Defined contribution pension costs	1.4	1.3
	<u>84.5</u>	<u>87.2</u>
Less charged to property, plant and equipment	<u>(41.7)</u>	<u>(41.3)</u>
	<u>42.8</u>	<u>45.9</u>

The majority of the Company's employees are members of the Northern Powergrid Group of the ESPS, details of which are given in Note 23.

The average monthly number of employees during the year was:

	2016 No.	2015 No.
Technical	322	316
Industrial	436	439
Administration	214	220
Other	103	100
	<u>1,075</u>	<u>1,075</u>

5 DIRECTORS' & KEY PERSONNEL REMUNERATION

DIRECTORS' REMUNERATION	2016 £	2015 £
<u>Highest Paid</u>		
Short-term employee benefits	207,345	288,251
Post-employment benefits	24,511	19,879
Other long-term benefits	321,769	262,387
	<u>553,625</u>	<u>570,517</u>
<u>Total</u>		
Short-term employee benefits	560,477	654,293
Post-employment benefits	84,864	79,691
Other long-term benefits	496,462	495,363
	<u>1,141,803</u>	<u>1,229,347</u>
Directors who are members of the defined benefit scheme	<u>3</u>	<u>4</u>
Accrued pension benefit relating to highest paid director	<u>-</u>	<u>-</u>

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NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

5 DIRECTORS' & KEY PERSONNEL REMUNERATION (CONTINUED)

OTHER KEY PERSONNEL REMUNERATION	2016 £	2015 £
<u>Total</u>		
Short-term employee benefits	368,261	211,239
Post-employment benefits	84,318	51,337
Other long-term benefits	227,320	92,697
	<u>679,899</u>	<u>355,273</u>

Other key personnel includes a number of senior functional managers who, whilst not board directors, have authority and responsibility for planning, directing and controlling the activities of the Company. During the year ended 31 March 2016, the senior management team was reorganised which resulted in additional senior functional managers being classed as key personnel.

The directors and key personnel are remunerated for their services to the Northern Powergrid Group, of which the Company is a subsidiary. The figures above represent the share of the costs borne by the Company.

6 OPERATING PROFIT

	2016 £m	2015 £m
This is stated after charging/(crediting):		
Staff costs (Note 4)	42.8	45.9
Research and Development	3.2	5.1
Depreciation of property, plant and equipment	72.6	65.1
Amortisation of deferred revenue	(21.7)	(20.1)
Amortisation of intangibles	2.8	1.9
Impairment loss on trade and other receivables	0.1	0.1
	<u>2016</u>	<u>2015</u>
Analysis of auditor's remuneration is as follows:	<u>£000</u>	<u>£000</u>
Fees payable to the Company's auditor for the audit of the Company's annual accounts	65	62
Other services supplied pursuant to legislation	40	38
Other assurance services	10	9
Other services	-	12

Other services supplied pursuant to legislation relate to regulatory reporting in line with Ofgem's requirements.

7 INVESTMENT INCOME

	2016 £m	2015 £m
Interest receivable from Group undertakings	<u>0.1</u>	<u>0.1</u>

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NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

8 FINANCE COSTS

	2016 £m	2015 £m
Interest payable on loans from Group undertakings	23.4	23.3
Interest payable on other loans	6.8	6.3
Total interest expense	30.2	29.6
Amounts included in the cost of qualifying assets	(3.1)	(3.7)
Total finance costs	27.1	25.9

9 INCOME TAX EXPENSE

	2016 £m	2015 £m
Analysis of tax expense		
Corporation tax	15.8	28.8
Deferred tax	(6.0)	3.8
Total tax expense in statement of profit or loss	9.8	32.6

The tax assessed for the year is lower than the standard rate of corporation tax in the UK. The difference is explained below:

	2016 £m	2015 £m
Profit on ordinary activities before income tax	116.8	157.8
The total charge can be reconciled to the accounting profit as follows: Profit on ordinary activities multiplied by the standard rate of corporation tax in the UK of 20% (2015 - 21%)	23.4	33.1
Effects of:		
Changes in legislation	(10.0)	-
Over provision for prior years	(3.0)	(0.5)
Other	(0.6)	-
Tax expense	9.8	32.6

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NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

9 INCOME TAX EXPENSE (CONTINUED)

	2016 £m	2015 £m
Tax expense comprises:		
Current tax expense:		
Corporation tax charge for the year	20.7	30.5
Over provision for prior years	(4.9)	(1.7)
Total current tax charge	15.8	28.8
Deferred tax:		
Deferred tax expenses relating to the origination and reversal of temporary differences	4.0	3.8
Effect of changes in legislation	(10.0)	-
Total deferred tax (credit)/charge	(6.0)	3.8
Tax on profit before tax	9.8	32.6

The Finance Act 2015 included provisions that the standard rate of corporation tax in the United Kingdom would reduce from 20% to 19% from April 2017 and to 18% from April 2020. Accordingly, the rate of 18% has been applied when calculating deferred tax assets and liabilities.

The Finance Bill 2016 legislates for the rate to reduce to 17% from April 2020. As this rate change had not been substantively enacted at the statement of financial position date this rate does not apply to the deferred tax position at 31 March 2016.

10 DIVIDENDS

	2016 Pence per share	2015 Pence per share	2016 £m	2014 £m
Dividend paid	10.3	15.0	20.6	30.0

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NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

11 PROPERTY, PLANT AND EQUIPMENT

	Distribution system	Fixtures and Equipment	Non- Operational Land & Buildings	Total
	£m	£m	£m	£m
COST				
At 1 April 2014	2,277.0	24.5	4.2	2,305.7
Additions	217.5	5.8	-	223.3
Disposals	(10.8)	(0.1)	-	(10.9)
At 1 April 2015	2,483.7	30.2	4.2	2,518.1
Additions	185.7	5.6	-	191.3
Disposals	(11.6)	(0.5)	-	(12.1)
At 31 March 2016	2,657.8	35.3	4.2	2,697.3
ACCUMULATED DEPRECIATION				
At 1 April 2014	413.2	20.5	1.3	435.0
Charge for the year	63.2	1.6	0.3	65.1
Disposals	(10.8)	(0.1)	-	(10.9)
At 1 April 2015	465.6	22.0	1.6	489.2
Charge for the year	69.5	2.8	0.3	72.6
Disposals	(11.6)	(0.5)	-	(12.1)
At 31 March 2016	523.5	24.3	1.9	549.7
Net book value at 31 March 2016	2,134.3	11.0	2.3	2,147.6
Net book value at 31 March 2015	2,018.1	8.2	2.6	2,028.9

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NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

11 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

Assets in the course of construction included above

	Distribution system	Fixtures and Equipment	Non- Operational Land & Buildings	Total
	£m	£m	£m	£m
At 1 April 2014	197.1	-	-	197.1
Additions	217.5	-	-	217.5
Available for use	<u>(240.2)</u>	<u>-</u>	<u>-</u>	<u>(240.2)</u>
At 1 April 2015	174.4	-	-	174.4
Additions	185.7	-	-	185.7
Available for use	<u>(198.1)</u>	<u>-</u>	<u>-</u>	<u>(198.1)</u>
At 31 March 2016	<u>162.0</u>	<u>-</u>	<u>-</u>	<u>162.0</u>

The net book value of non-operational land and buildings comprises:

	2016 £m	2015 £m
Freehold	1.7	2.0
Long-leasehold	<u>0.6</u>	<u>0.6</u>
	<u>2.3</u>	<u>2.6</u>

The Company has entered into contractual commitments in relation to the future acquisition of property, plant and equipment of £29.4m (2015: £32.2m).

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NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)**12 INTANGIBLE ASSETS**

	Software Development Costs £m
COST	
At 1 April 2014	38.6
Additions	10.3
	<hr/>
At 1 April 2015	48.9
Additions	9.8
	<hr/>
At 31 March 2016	58.7
	<hr/>
AMORTISATION	
At 1 March 2014	20.4
Charge for the year	1.9
	<hr/>
At 1 April 2015	22.3
Charge for the year	2.8
	<hr/>
At 31 March 2016	25.1
	<hr/>
Net book value at 31 March 2016	33.6
	<hr/>
Net book value at 31 March 2015	26.6
	<hr/>

13 INVESTMENTS

Details of the investments held by the Company as at 31 March 2016 are listed below:

Name of Company	Country of Registration	Holding of Ordinary Shares	Proportion	Nature of Business
Electralink Limited	England and Wales	619 at 10p	6.7%	Data transfer network operator
MRA Service Company Limited	England and Wales	1 at £1	1.0%	Governance of the electricity industry's Master Registration Agreement
DCUSA Limited	England and Wales	1 at £1	1.7%	Management and governance of the Distribution Connection and Use of System Agreement
Smart Energy Code Company Limited	England and Wales	1 at £1	0.9%	Management and governance of the Smart Energy Code
Northern Electric Finance plc	England and Wales	50,000 at £1	100%	Finance company

The above investments are unlisted. The cost and net book value of the investments are Electralink Limited £62 (2015: £62), MRA Service Company Limited £1 (2015: £1), DCUSA Limited £1 (2015: £1), Smart Energy Code Company Limited £1 (2015: £Nil) and Northern Electric Finance plc £50,000 (2015: £50,000). The registered office address of Northern Electric Finance plc is Lloyds Court, 78 Grey Street, Newcastle upon Tyne, NE1 6AF.

NORTHERN POWERGRID (NORTHEAST) LIMITED**REGISTERED NUMBER 02906593****NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)****14 INVENTORIES**

	2016 £m	2015 £m
Raw materials and consumables	11.4	11.8
Work in progress	0.2	0.3
	<u>11.6</u>	<u>12.1</u>

15 TRADE AND OTHER RECEIVABLES

	2016 £m	2015 £m
Distribution use of system receivables	44.8	53.3
Amounts receivable from sale of goods and services	5.5	1.8
Prepayments and accrued income	1.2	1.2
Other receivables	3.2	1.7
	<u>54.7</u>	<u>58.0</u>

The directors consider that the carrying amount of trade and other receivables approximates their fair value calculated by discounting the future cash flows at the market rate at the statement of financial position date. The maximum exposure to risk to the Company is the book value of these receivables less any provisions for impairment. The fair valuation of assets is based on Level 1 inputs.

Distribution use of system receivables

The customers served by the Company's distribution network are supplied predominantly by a small number of electricity supply businesses with RWE NPower plc accounting for approximately 23% of distribution revenues in the regulatory year to 31 March 2016 (2015: 27%). Ofgem has determined a framework which sets credit limits for each supply business based on its credit rating or payment history and requires them to provide credit cover if their value at risk (measured as being equivalent to 45 days usage) exceeds the credit limit. Acceptable credit typically is provided in the form of a parent company guarantee, letter of credit or an escrow account. Included within other payables are customer deposits of £0.4m as at 31 March 2016 (2015: £1.7m).

Ofgem has indicated that, provided the Company has implemented credit control, billing and collection processes in line with best practice guidelines and can demonstrate compliance with the guidelines or is able to satisfactorily explain departure from the guidelines, any bad debt losses arising from supplier default will be recovered through an increase in future allowed income. Losses incurred to date have not been material. Included in the Company's use of system ("UoS") receivables are debtors with a carrying value of £Nil, which have been placed into administration. Consequently, no provision was required at the regulatory year-end (2015: £Nil)

Amounts receivable from sale of goods and services

Sales of goods and services comprise all income streams which are not classified as UoS income. Examples of non-UoS income streams would be service alterations/disconnections and recovery of amounts for damage caused by third parties to the distribution system.

The average credit period on sales of goods and services is 30 days. Interest is not generally charged on the trade receivables paid after the due date. An allowance for doubtful debts is made for debts past their due date based on estimated irrecoverable amounts from the sale of goods and services, determined by reference to past default experience.

NORTHERN POWERGRID (NORTHEAST) LIMITED**REGISTERED NUMBER 02906593****NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)****15 TRADE AND OTHER RECEIVABLES (CONTINUED)****Amounts receivable from sale of goods and services (continued)**

Included in the Company's amounts receivable for goods and services balance are debtors with a carrying amount of £1.1m (2015: £0.9m) which are past due at the reporting date and for which the Company has provided an irrecoverable amount of £0.2m (2015: £0.3m) based on past experience. The Company does not hold any collateral over these balances. The average age of these receivables is 219 days (2015: 398 days).

Included in the Company's amounts receivable for goods and services balance are debtors with a carrying amount of £0.8m (2015: £0.2m). These amounts are past due at the reporting date and the Company has not provided for any amounts as not being recoverable because there has not been a significant change in credit quality and the amounts are still considered recoverable. The Company does not hold any collateral over these balances. The average age of these receivables is 87 days (2015: 98 days).

Ageing of past due but not impaired receivables

	2016 £m	2015 £m
30-60 days	0.1	0.1
120-210 days	-	0.1
Total	<u>0.1</u>	<u>0.2</u>

Movement in the allowance for doubtful debts

	£m	£m
At 1 April	0.3	0.4
Amounts recognised in statement of profit or loss	0.1	0.1
Amounts utilised/written off in the year	<u>(0.2)</u>	<u>(0.2)</u>
At 31 March	<u>0.2</u>	<u>0.3</u>

In determining the recoverability of the trade and other receivables, the Company considers any change in the credit quality of the trade and other receivables from the date credit was initially granted up to the reporting date. The concentration of credit risk, other than in relation to UoS receivables, is limited due to the customer base being large and unrelated. Accordingly, the directors believe that no further credit provision is required in excess of the allowance for doubtful debts.

Included in the allowance for doubtful debts are specific trade receivables, with a balance of £0.1m (2015: £0.2m), for companies which have been placed in administration. The impairment represents the difference between the carrying amount of the specific trade receivable and the present value of the expected liquidation dividend.

NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)**15 TRADE AND OTHER RECEIVABLES (CONTINUED)****Categories of financial assets**

	2016 £m	2015 £m
Loans and receivables at amortised cost	53.5	56.8
Total financial assets	<u>53.5</u>	<u>56.8</u>
Non-current assets	2,181.2	2,055.5
Inventories	11.6	12.1
Prepayments and accrued income	1.2	1.2
Total non-financial assets	<u>2,194.0</u>	<u>2,068.8</u>
Total Assets	<u>2,247.5</u>	<u>2,125.6</u>

16 OTHER FINANCIAL LIABILITIES**Trade and other payables**

	2016 £m	2015 £m
Payments received on account	50.0	40.2
Trade payables	8.4	4.9
Amounts owed to Group undertakings (Note 25)	0.7	0.9
Other taxes and social security costs	3.3	3.4
Accruals	27.3	51.0
Other payables	5.1	5.4
	<u>94.8</u>	<u>105.8</u>

Current income tax liabilities

	2016 £m	2015 £m
Corporation tax	<u>4.5</u>	<u>13.5</u>

The directors consider that the carrying amount of other financial liabilities approximates their fair value, calculated by discounting future cash flows at market rate at the statement of financial position date. The fair valuation of liabilities is based on Level 1 inputs. Trade creditors and accruals principally comprise amounts outstanding for trade purchases and ongoing costs. Invoices are paid at the end of the month following the date of the invoice. The Company has financial risk management policies in place to ensure that all payables are paid within the credit timeframe.

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NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

16 OTHER FINANCIAL LIABILITIES (CONTINUED)

The following tables detail the remaining contractual maturities for the non-derivative financial liabilities included in Notes 16 and 17. The tables have been drawn up based on the undiscounted cash flows of financial liabilities based on the earliest possible date on which the Company can be required to pay. The tables include both interest and principal cash flows.

	Less than 3 months £m	3 months To 1 year £m	1 to 5 Years £m	5+ Years £m	Total £m
2016:					
Non-interest bearing	44.5	-	-	-	44.5
Variable interest rate liability	56.9	-	-	-	56.9
Fixed interest rate liability	2.6	28.0	331.3	617.4	979.3
	104.0	28.0	331.3	617.4	1,080.7
2015:					
Non-interest bearing	65.6	-	-	-	65.6
Variable interest rate liability	143.1	-	-	-	143.1
Fixed interest rate liability	2.6	24.9	224.0	598.3	849.8
	211.3	24.9	224.0	598.3	1,058.5

Categories of financial liabilities

	2016 £m	2015 £m
Loans and payables at amortised cost	668.8	631.0
Total financial liabilities	668.8	631.0
Payments received on account	50.0	40.2
Income tax liabilities	100.0	115.0
Other taxes and social security	3.3	3.4
Accruals	27.3	51.0
Deferred revenue	553.4	526.6
Provisions	1.5	1.6
Total non-financial liabilities	735.5	737.8
Total liabilities	1,404.3	1,368.8

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NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

17 BORROWINGS

The Directors' consideration of liquidity, interest rate and foreign currency risk is described in the Strategic Report on pages 5 and 6.

	Book value		Fair value	
	2016	2015	2016	2015
	£m	£m	£m	£m
Loans	240.5	192.9	252.9	204.9
Amounts owed to Group undertakings	414.1	426.9	513.8	541.9
	654.6	619.8	766.7	746.8
The borrowings are repayable as follows:				
On demand or within one year	67.7	153.0	67.7	153.0
After one years	586.9	466.8	699.0	593.8
	654.6	619.8	766.7	746.8
Analysis of borrowings:				
Short-term loan	-	73.3	-	73.3
Inter-company short-term loan	56.9	69.8	56.9	69.8
Northern Electric Finance plc 2020 – 8.875%	104.1	104.1	133.8	138.3
Northern Electric Finance plc 2035 – 5.125%	50.3	50.2	63.3	65.0
Yorkshire Electricity Group plc 2037 – 5.9%	101.5	101.5	135.8	140.6
Northern Electric Finance plc 2037 – 5.125%	101.3	101.3	124.0	128.2
European Investment Bank 2018 – 4.065%*	40.2	40.2	42.4	43.2
European Investment Bank 2019 – 4.241%*	40.2	40.2	43.7	44.3
European Investment Bank 2020 – 4.386%*	39.2	39.2	43.8	44.1
European Investment Bank 2027 – 2.564%	120.9	-	123.0	-
	654.6	619.8	766.7	746.8

The fair value of the bonds is determined with reference to quoted market prices. The directors' estimates of the fair value of bank loans and internal borrowings are determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions or dealer quotes for similar instruments. The fair value of short-term borrowings is equal to their book value. All loans are non-secured and are denominated in sterling.

* The 2018, 2019 and 2020 borrowings from the European Investment Bank were drawn down in twelve tranches. The interest rates shown above are average rates for those repayment dates. The spread of interest rates is as follows:

2018: 3.901% - 4.283%
 2019: 4.077% - 4.455%
 2020: 4.227% - 4.586%

Interest on short-term loans and inter-company short term loans is charged at a floating rate of LIBOR plus 0.35%, thus exposing the Company to cash flow interest rate risk. A 1% movement in interest rates would subject the Company to an approximate change in interest costs of £1.4m per year. This is considered to be an acceptable level of risk. All other loans are at fixed interest rates and expose the Company to fair value interest rate risk.

The loans are non-secured and are denominated in sterling.

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NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

17 BORROWINGS (CONTINUED)

The covenants associated with the 2035 bonds issued by Northern Electric Finance plc, a wholly-owned subsidiary of the Company, include restrictions on the issuance of new indebtedness and the making of distributions dependent on the scale of the ratio of Senior Total Net Debt to Regulatory Asset Value ("RAV").

The definition of Senior Total Net Debt excludes any subordinated debt and any debt incurred on a non-recourse basis. In addition, it excludes interest payable, any fair value adjustments and unamortised issue costs.

The Company's Senior Total Net Debt as at 31 March 2016 totalled £644.4m. Using the RAV value as at March 2016, as outlined by Ofgem in its electricity distribution price control financial model published in November 2015, and adjusting for the effects of movements in the value of the Retail Prices Index ("RPI") gives an approximation for the RAV value as at 31 March 2016 of £1,247.8m. The Senior Total Net Debt to RAV ratio for the Company is therefore estimated at 51.6% (2015: 51.9%).

At 31 March 2016, the Company had available £94.0m (2015: £20.7m) of undrawn committed borrowing facilities in respect of which all conditions precedent had been met.

18 DEFERRED TAX

	Accelerated Tax Depreciation £m	Other £m	Total £m
At 1 April 2014	97.9	(0.2)	97.7
Charge to statement of profit or loss	3.8	-	3.8
At 1 April 2015	101.7	(0.2)	101.5
Credit to statement of profit or loss	(6.0)	-	(6.0)
At 31 March 2016	95.7	(0.2)	95.5

Other comprises provisions and employee expenses deductible for tax on a paid basis and claims for hold over relief.

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NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

19 DEFERRED REVENUE

	2016 £m	2015 £m
At 1 April 2015	526.6	510.7
Additions	48.5	36.0
Amortisation	(21.7)	(20.1)
	<u>553.4</u>	<u>526.6</u>
At 31 March 2016		
	2016 £m	2015 £m
Included in current liabilities	20.1	21.3
Included in non-current liabilities	533.3	505.3
	<u>553.4</u>	<u>526.6</u>

Deferred revenue represents contributions from customers made in advance towards distribution system assets. This income is released to the statement of profit or loss up to 45 years on a straight line basis in line with the useful economic life of the distribution system assets.

20 PROVISIONS

	Claims £m	Other £m	Total £m
At 1 April 2015	1.1	0.8	1.9
Utilised/paid in the year	(0.7)	-	(0.7)
Charged to the statement of profit or loss	<u>0.3</u>	<u>0.1</u>	<u>0.4</u>
At 1 April 2015	0.7	0.9	1.6
Utilised/paid in the year	(0.6)	(0.4)	(1.0)
Charged to statement of profit or loss	<u>0.8</u>	<u>0.1</u>	<u>0.9</u>
At 31 March 2016	<u>0.9</u>	<u>0.6</u>	<u>1.5</u>
	2016 £m	2015 £m	
Included in current liabilities	1.2	1.3	
Included in non-current liabilities	0.3	0.3	
	<u>1.5</u>	<u>1.6</u>	

Claims: Provision has been made to cover costs arising from actual claims, which are not externally insured. Settlement is expected substantially within 12 months.

Other: Primarily consists of a provision for future safe disposal of transformers which contain oil contaminated with Polychlorinated Biphenyls (PCBs) and for an amount to cover claims made under section 74 of the New Road and Street Works Act 1991. Costs are expected to be incurred over the next 15 years.

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NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

21 SHARE CAPITAL

	2016 No./£	2015 No./£
Ordinary shares of £1 each		
Allotted, called-up and fully paid	<u>200,000,100</u>	<u>200,000,100</u>

The Company has one class of ordinary shares which carries no right to fixed income.

22 RECONCILIATION OF PROFIT BEFORE INCOME TAX TO CASH GENERATED FROM OPERATIONS

	2016 £m	2015 £m
Profit before income tax	116.7	157.8
Depreciation and amortisation	75.4	67.0
Profit on disposal of fixed assets	(0.5)	(0.7)
Amortisation of deferred revenue	(21.7)	(20.1)
Decrease in provisions	(0.1)	(0.3)
Interest receivable		-
Finance costs	27.1	25.9
Investment income	<u>0.0</u>	<u>(0.1)</u>
Operating cash flows before movements in working capital	196.9	229.5
Decrease/(increase) in inventories	0.5	(2.5)
Decrease/(increase) in receivables	5.1	(7.4)
Decrease in payables	<u>(5.7)</u>	<u>(0.5)</u>
Cash generated from operations	<u>196.8</u>	<u>219.1</u>

NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

23 PENSION COMMITMENTS

Introduction

The Company contributes to two pension schemes, which are operated by Northern Electric plc on behalf of the participating companies within the Northern Powergrid Group. Those pension schemes are:

- The Northern Powergrid Group of the ESPS (the "DB Scheme"); and
- The Northern Powergrid Pension Scheme.

The Northern Powergrid Pension Scheme was introduced for new employees of the Northern Powergrid Group from July 1997 and is a money purchase arrangement accounted for as a defined contribution scheme.

The DB Scheme is a defined benefit scheme for directors and employees, which provides pension and other related retirement benefits based on final pensionable pay. The DB Scheme closed to staff commencing employment with the Northern Powergrid Group on or after 23 July 1997. Members who joined before this date, including some Protected Persons under The Electricity (Protected Persons) (England and Wales) Pension Regulations 1990, continue to build up future pension benefits.

Under the DB Scheme, employees are typically entitled to annual pensions on retirement at age 63 of one-eightieth of final pensionable salary for each year of service plus an additional tax-free cash lump sum at retirement of three times pension. Benefits are also payable on death and following other events such as withdrawing from active service.

No other post-retirement benefits are provided to members of the DB Scheme.

The DB Scheme is a defined benefit plan that shares the risk between various entities under common control. There is no contractual agreement or stated policy for charging the defined benefit cost for the plan as a whole to individual companies within the Northern Powergrid Group and, accordingly, the Company accounts for the DB Scheme as if it were a defined contribution scheme.

Unless otherwise stated, disclosures within this note are representative of the Northern Powergrid Group as a whole and not the Company on an individual basis as the Company accounts for the DB Scheme as if it were a defined contribution scheme.

Role of Trustees

The DB Scheme is administered by a board of Trustees which is legally separate from the Company. The assets of the DB Scheme are held in a separate trustee-administered fund. The board of Trustees is made up of Trustees appointed by Northern Electric plc, as the Principal Employer of the DB Scheme, Trustees elected by the membership and an independent trustee. The Trustees are required by law to act in the interests of all relevant beneficiaries and are responsible in particular for the asset investment strategy plus the day-to-day administration of the benefits payable. They also are responsible for jointly agreeing with the Principal Employer the level of contributions due to the DB Scheme.

NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

23 PENSION COMMITMENTS (CONTINUED)

Funding requirements

UK legislation requires that pension schemes are funded prudently (i.e. to a level in excess of the current expected cost of providing benefits). The last actuarial valuation of the DB scheme was carried out by the Trustees' actuarial advisors, Aon Hewitt, as at 31 March 2013. Such valuations are required by law to take place at intervals of no more than three years. Following each valuation, the Trustees and the Northern Powergrid Group must agree the contributions required (if any) to ensure the DB Scheme is fully funded over time on the basis of suitable, prudent assumptions. Contributions agreed in this manner constitute a minimum funding requirement. The current funding valuation is taking place as at 31 March 2016, as part of which the funding position will be reviewed.

Agreement was reached during October 2014 with the Trustees to repair the funding deficit of £286.4m as at 31 March 2013 over the 11 year period to 31 March 2025, subject to the actuarial assumptions adopted for the triennial valuation as at 31 March 2013 being borne out in practice. The agreement includes cash payments, made on a monthly basis, of £34.9m per annum over the period to 31 March 2015 and £28.6m over the year to 31 March 2016 (of which £19.0m was borne by the Company), followed by payments of £18.4m per annum to be made over the remaining ten years of the recovery plan.

All contributions set out above are in 2014/15 prices and will be increased each year in line with increases in RPI over the period until they fall due.

The contributions payable by the Northern Powergrid Group to the DB Scheme in respect of future benefits, which are accruing, are 34.2% of pensionable pay. These contributions were determined as part of the 31 March 2013 actuarial valuation and are payable in addition to the deficit repair contributions mentioned above. These rates will remain in place until such a time as a new schedule of contributions is agreed between the Trustees and Northern Electric plc as part of the 31 March 2016 valuation. In addition, the Company pays 3.0% of pensionable pay to the DB Scheme in respect of the expenses of running the DB Scheme.

Under the rules of the DB Scheme, any future surplus in the DB Scheme may, following consultation with the Group Trustees, be allocated for the benefit of the members of the DB Scheme and/or the Principal and Participating Employers.

NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

23 PENSION COMMITMENTS (CONTINUED)

Pensions' Regulation

The UK pensions market is regulated by the Pensions Regulator whose key statutory objectives in relation to UK defined benefit plans are to:

- protect the benefits of members;
- promote and to improve understanding of good administration;
- reduce the risk of situations arising which may lead to compensation being payable from the Pension Protection Fund ("PPF"); and
- minimise any adverse impact on the sustainable growth of an employer.

The Pensions Regulator has various powers including the power to:

- wind up a scheme where winding up is necessary to protect members' interests;
- appoint or remove a trustee;
- impose a schedule of company contributions or the calculation of the technical provisions where trustees and company fail to agree on appropriate contributions; and
- impose contributions where there has been a detrimental action against the scheme.

Profile of the DB Scheme

The Defined Benefit Obligation ("DBO") includes benefits for current employees, former employees and current pensioners. The overall duration of the DB Scheme's obligation was assessed to be about 17 years based on the results of the 31 March 2013 funding valuation. This is the weighted-average time over which benefit payments are expected to be made.

Broadly, about 40% of the liabilities are attributable to current employees (duration about 23 years), 10% to former employees (duration about 24 years) and 50% to current pensioners (duration about 12 years).

Risks associated with the DB Scheme

The DB Scheme exposes the Northern Powergrid Group to a number of risks, the most significant of which are:

Risk	Description	Mitigation
Volatile asset returns	The DBO is calculated using a discount rate set with reference to corporate bond yields. If assets underperform this discount rate, this will create an element of deficit. The DB Scheme aims to hold a significant proportion (48%) of its assets in growth assets (such as equities) which, although expected to outperform corporate bonds in the long-term, create volatility and risk in the short-term.	The allocation to growth assets is monitored to ensure it remains appropriate given the DB Scheme's long-term objectives. The Trustees regularly review the strategy from growth seeking assets and have diversified some return-seeking assets from equities into Reinsurance and Listed Infrastructure to reduce overall risk. To avoid concentration risk, the allocation to UK equity is restricted to 35% of the total equity allocation.

NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)**23 PENSION COMMITMENTS (CONTINUED)**

Risk	Description	Mitigation
Changes in bond yields	A decrease in corporate bond yields will increase the value placed on the DBO for accounting purposes, although this will be partially offset by an increase in the value of the DB Scheme's bond holdings.	The DB Scheme also holds a substantial proportion of its assets (52%) as bonds, which provide a hedge against falling bond yields (falling yields which increase the DBO will also increase the value of the bond assets). There are some differences in the credit quality of bonds held by the DB Scheme and the bonds analysed to decide the DBO discount rate, such that there remains some risk should yields on different quality bond/swap assets diverge.
Inflation risk	A significant proportion of the DBO is indexed in line with price inflation (specifically in line with RPI) and higher inflation will lead to higher liabilities.	The DB Scheme holds around 30% in UK government index-linked bonds which provide a hedge against higher than expected inflation increases of the DBO (rising inflation will increase both the DBO and the value of the index-linked bond portfolio).
Currency risk	To increase diversification, the DB Scheme invests in overseas assets. This leads to a risk that foreign currency movements negatively impact the value of assets in Sterling terms.	The DB Scheme hedges a proportion of the overseas investments currency risk for those overseas currencies that can be hedged efficiently. The DB Scheme's currency hedging ratio is currently 50% in respect of overseas developed market currencies.
Life expectancy	The majority of the DB Scheme's obligations are to provide benefits for the pensionable lifetime of the member, so increases in life expectancy will result in an increase in the liabilities.	The DB Scheme regularly reviews actual experience of its membership against the actuarial assumptions underlying the future benefit projections and carries out detailed analysis when setting an appropriate scheme specific mortality assumption.

The Northern Powergrid Group and Trustees have agreed a long-term strategy for reducing investment risk as and when appropriate. This includes an element of asset-liability matching, which aims to reduce the volatility of the funding level of the DB Scheme by investing in certain assets, which perform in line with the liabilities of the DB Scheme.

Other risks

There are a number of other risks associated with the DB Scheme including operational risks (such as paying out the wrong benefits), legislative risks (such as the government increasing the burden on pension schemes through new legislation) and other demographic risks (such as a higher proportion members dying than assumed with a dependant eligible to receive a survivor's pension from the DB Scheme).

A particular legislative risk exists in relation to the equalisation of the Guaranteed Minimum Pension ("GMP"), a quasi-state benefit accrued by many UK plans over the period 1978 to 1997 as a result of a UK government programme allowing pension plans to "contract out" of the State Second Pension. The UK Government has announced its intention to ensure that these benefits, which currently pay out at different levels for men and women, are gender-equalised in accordance with sex-discrimination legislation. This would increase the DBO but it is not possible to fully quantify the impact of this change at this stage. However, it could lead to an increase in the order of 2% to the DBO for a typical scheme.

NORTHERN POWERGRID (NORTHEAST) LIMITED**REGISTERED NUMBER 02906593****NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)****23 PENSION COMMITMENTS (CONTINUED)****Reporting at 31 December 2015**

For the purposes of this disclosure, the current and future pension costs of the Northern Powergrid Group have been assessed by Aon Hewitt, a qualified independent actuary, using the assumptions set out below, which the actuary has confirmed represent a reasonable best estimate of those costs. This review has been based on the same membership and other data as at 31 March 2013. The board of Northern Powergrid Holdings Company has accepted the advice of the actuary and formally approved the use of these assumptions for the purpose of calculating the pension cost of the Northern Powergrid Group.

The results of the latest funding valuation at 31 March 2013 have been adjusted to 31 December 2015. Those adjustments take account of experience over the period since 31 March 2013, changes in market conditions, and differences in the financial and demographic assumptions. The present value of the DBO and the related current service cost were measured using the Projected Unit Credit Method.

For schemes closed to new members, such as the DB Scheme, the current service cost calculated under the Projected Unit Credit Method is expected to increase as the members of the scheme approach retirement.

The Company's total DB pension cost for the year ended 31 March 2016 was £28.2m (2015: £32.2m).

The principal assumptions used to calculate the liabilities under IAS 19 are set out below:

Main financial assumptions	December 2015	December 2014
	% p.a.	% p.a.
RPI Inflation	2.90	2.80
Rate of long-term increase in salaries	2.90	2.80
Pension increases	2.80	2.70
Discount rate for scheme liabilities	2.70	3.60

The financial assumptions reflect the nature and term of the DB Scheme's liabilities.

Main demographic assumptions	December 2015	December 2014
Life expectancy for a male currently aged 60	27.0	27.1
Life expectancy for a female currently aged 60	28.7	28.9
Life expectancy at 60 for a male currently aged 45	28.5	28.7
Life expectancy at 60 for a female currently aged 45	30.4	30.6
Proportion of pension exchanged for additional cash at retirement	10%	10%

The mortality assumptions are based on recent actual mortality experience of DB Scheme members and allow for expected future improvements in mortality rates.

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NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

23 PENSION COMMITMENTS (CONTINUED)

The DB Scheme's funds are invested in the following assets:

Asset allocation	December 2015 £m	December 2014 £m
Developed market equity	311.0	306.2
Emerging market equity	11.2	12.6
Property	146.0	130.3
Reinsurance	68.2	64.5
Listed infrastructure	90.1	84.7
Investment grade corporate bonds	375.5	343.1
Other debt	38.7	57.4
Fixed interest gilts	24.9	28.5
Index-linked gilts	453.7	452.7
Cash	22.0	36.0
Total	1,541.3	1516.1

The fair values of the above equity and debt instruments are determined based on quoted market prices in active markets whereas the fair values of properties are not based on quoted prices in active markets.

As at 31 December 2015, the fair value of the DB Scheme's assets, which related to self-investment, amounted to Nil% (2014: Nil%).

Changes to the present value of the DBO during the year	December 2015 £m	December 2014 £m
Opening DBO	1,463.2	1,321.3
Current service cost	15.9	14.5
Interest expense on defined benefit obligation	52.0	57.3
Contributions by DB Scheme participants	1.5	1.5
Actuarial gains on DB Scheme liabilities arising from changes in demographic assumptions	(12.4)	(19.2)
Actuarial (gains)/losses on DB Scheme liabilities arising from changes in financial assumptions	(1.9)	110.4
Actuarial (gains)/losses on DB Scheme liabilities arising from experience	(5.6)	33.3
Net benefits paid out	(59.5)	(55.9)
Closing DBO	1,453.2	1,463.2

Changes in the fair value of DB Scheme assets of the Northern Powergrid Group during the year	December 2015 £m	December 2014 £m
Opening fair value of DB Scheme assets	1,516.1	1,310.7
Interest income on DB Scheme assets	54.5	57.6
Re-measurement (losses)/gains on DB Scheme assets	(20.3)	149.6
Contributions by the employer	50.2	54.1
Contributions by DB Scheme participants	1.5	1.5
Net benefits paid out	(59.5)	(55.9)
Administration costs incurred	(1.2)	(1.5)
Closing fair value of DB Scheme assets	1,541.3	1,516.0

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NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

23 PENSION COMMITMENTS (CONTINUED)

Actual return on DB Scheme assets	December 2015 £m	December 2014 £m
Interest income on DB Scheme assets	54.5	57.6
Re-measurement (losses)/gain on DB Scheme assets	(20.3)	149.6
Actual return on DB Scheme assets	34.2	207.2

Sensitivity to key assumptions

The key assumptions used for IAS 19 are discount rate, inflation and mortality. If different assumptions were used, it could have a material effect on the results of the Northern Powergrid Group. The sensitivity of the results to these assumptions is as follows.

	Changes in DBO £'000	Revised DBO £'000
Current Figures	1,453.2	
Following a 10 bps decrease in the discount rate	25.9	1,489.3
Following a 10 bps increase in the discount rate	(25.6)	1,437.5
Following a 10 bps increase in the inflation assumption	23.1	1,487.5
Following a 10 bps decrease in the inflation assumption	(21.3)	1,439.2
Following a 1 year increase in life expectancy	49.5	1,511.5
Following a 1 year decrease in life expectancy	(50.1)	1,414.4

The sensitivity information shown above has been prepared using the same method as adopted when adjusting the results of the latest funding valuation to the statement of financial position date. This is the same approach as has been adopted in previous periods.

24 OPERATING LEASE ARRANGEMENTS

	2016 £m	2015 £m
Minimum lease payments under operating leases recognised in the year	6.2	6.3

At the statement of financial position date, the Company had outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows:

	2016 £m	2015 £m
Within one year	4.7	4.7
In the second to fifth year inclusive	15.7	14.8
After five years	5.4	1.6
	25.8	21.1

Leases consist of rent payable in respect of properties and vehicle leases (both primarily from related parties).

NORTHERN POWERGRID (NORTHEAST) LIMITED**REGISTERED NUMBER 02906593****NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)****25 RELATED PARTY TRANSACTIONS**

The Company has advanced loans to companies in the Northern Powergrid Group. The total interest included in investment income in the statement of profit or loss for the year ended 31 March 2016 was £0.1m (2015: £0.1m).

The Company has received loans from other companies in the Northern Powergrid Group. The total interest included in finance costs in the statement of profit or loss for the year ended 31 March 2016 was £23.4m (2015: £23.3m). Included within borrowings is £414.1m as at 31 March 2016 (2015: £426.9m).

Interest on loans to/from Northern Powergrid Group companies is charged at a commercial rate.

The Company entered into transactions, in the ordinary course of business, with affiliated companies. Transactions entered into and trading balances outstanding at the regulatory year-end were as follows:

Related Party	Sales to Related Party	Purchases from Related Party	Amounts Owed to Related Party (Note 16)
	£m	£m	£m
2016:			
Northern Powergrid Insurance Services Limited		0.2	
Integrated Utility Services Limited	0.3	2.2	
Integrated Utility Services Limited (registered in Eire)		1.2	0.3
Northern Electric plc		7.2	
Northern Powergrid (Yorkshire) plc	18.5	11.2	-
Vehicle Lease and Service Limited	-	3.8	0.4
2015:			
Northern Powergrid Insurance Services Limited	-	0.4	-
Integrated Utility Services Limited	0.3	1.7	-
Integrated Utility Services Limited (registered in Eire)	-	1.4	0.5
Northern Electric plc	0.1	7.0	-
Northern Powergrid Metering Limited	0.1	-	-
Northern Powergrid (Yorkshire) plc	17.1	10.7	-
Vehicle Lease and Service Limited	-	3.7	0.4

Sales and purchases from related parties were made at commercial prices.

The amounts outstanding are unsecured and will be settled in cash. No guarantees have been given or received. No provisions have been made for doubtful debts in respect of amounts owed by related parties

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NOTES TO THE REGULATORY ACCOUNTS FOR THE YEAR ENDED 31 MARCH 2016 (CONTINUED)

26 IMMEDIATE PARENT UNDERTAKING AND CONTROLLING PARTY

The immediate parent undertaking of Northern Powergrid (Northeast) Limited is Northern Electric plc. The ultimate controlling party and ultimate parent undertaking of Northern Electric plc is Berkshire Hathaway, Inc., a company incorporated in the United States of America.

Copies of the group accounts of Berkshire Hathaway, Inc. (the parent undertaking of the largest group preparing group accounts) which include Northern Powergrid (Northeast) Limited and the group accounts of Northern Electric plc, the smallest parent undertaking to prepare group accounts in the United Kingdom, can both be obtained from the Company Secretary, Northern Powergrid Holdings Company, Lloyds Court, 78 Grey Street, Newcastle upon Tyne, NE1 6AF.