

NORTHERN ELECTRIC plc
HALF-YEARLY FINANCIAL REPORT
SIX MONTHS ENDED 30 JUNE 2016

NORTHERN ELECTRIC plc

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NORTHERN ELECTRIC plc
(REGISTERED NUMBER: 02366942)

INTERIM MANAGEMENT REPORT

Registered in England and Wales
Registered Office: Lloyds Court, 78 Grey Street, Newcastle upon Tyne, NE1 6AF

Cautionary Statement

This interim management report has been prepared solely to provide additional information to shareholders to assess the business strategies of Northern Electric plc (the “Company”) and its subsidiaries (together the “Group”) and the potential for those strategies to succeed and should not be relied on by any other party or for any other purpose.

Review of the six months to 30 June 2016

The Company is part of the Northern Powergrid Holdings Company group of companies (the “Northern Powergrid Group”) and its principal activity during the six months to 30 June 2016 was to act as a holding company, with its main operating subsidiaries being Northern Powergrid (Northeast) Limited (“Northern Powergrid”), Integrated Utility Services Limited (“IUS”) and Northern Powergrid Metering Limited (“Metering”).

Northern Powergrid distributes electricity to approximately 1.6 million customers connected to its electricity distribution network in the North East of England and is an authorised distributor under the Electricity Act 1989. IUS provides engineering contracting services to various clients and Metering rents smart meters to energy suppliers. The Group operates a business model and strategy based on the Northern Powergrid Group’s core principles, details of which can be found in the Group’s annual reports and accounts for the year ended 31 December 2015.

Financial strength

Results for the six months ended 30 June 2016

The half-yearly accounts for the six months ended 30 June 2016 consolidate the results of the Group and are prepared under International Financial Reporting Standards. The half-yearly accounts do not comprise statutory accounts required to be delivered to the Registrar of Companies under the Companies Act 2006 and have not been subject to audit or review by the Group’s auditor. The Group will deliver its statutory accounts for the current financial year ending on 31 December 2016 to the Registrar of Companies by 30 June 2017.

The Group delivered a satisfactory performance for the six months ended 30 June 2016, although profit after tax reduced by £11.1 million when compared to the previous year mainly as a result of lower revenue, the reasons for which are set out below, and higher depreciation charges. A summary of the key financial results is as follows:

Key financials

Revenue

Revenue at £190.0 million was £10.6 million lower than for the six months ended 30 June 2015 mainly due to receipt of lower Distribution Use of System revenues by Northern Powergrid, offset by higher smart meter rental income.

INTERIM MANAGEMENT REPORT (CONTINUED)

Key financials (continued)

Cash flow

Cash and cash equivalents as at 30 June 2016 were £Nil, representing a decrease of £8.8 million when compared with the position at 31 December 2015.

Northern Powergrid has access to £75.0 million under a five-year committed revolving credit facility provided by Lloyds Bank plc, Royal Bank of Scotland plc and Abbey National Treasury Services plc, which is due to expire on 30 April 2020.

In addition, the Group has access to short-term borrowing facilities provided by Yorkshire Electricity Group plc, a related party, and to a £22 million overdraft facility provided by Lloyds Bank plc.

Financial position

Profit before tax at £75.0 million was £15.0 million lower than the six months ended 30 June 2015 mainly as a result of lower revenues and higher depreciation.

Dividends

No ordinary dividends were paid in the period resulting in £59.6 million being transferred to reserves.

Related party transactions

The Company provides certain corporate functions to the Northern Powergrid Group, including financial accounting and planning, treasury, taxation, pensions, internal audit, legal advice, insurance management, claims handling and litigation services.

Further details of the related party transactions entered into by the Group and the Company and changes therein are included in Note 8 to this half-yearly financial report.

Customer service

Northern Powergrid's key customer service performance indicators are customer interruptions ("CI") and customer minutes lost ("CML") and, for the regulatory year to 31 March 2016 (the "Regulatory Year"), both indicators were better than Ofgem's targets. As at the date of this half-yearly financial report, Northern Powergrid'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

INTERIM MANAGEMENT REPORT (CONTINUED)

Customer service (continued)

Under the Broad Measure of Customer Satisfaction, an independent market research company carries out telephone surveys with Northern Powergrid's customers to find out how satisfied they were with the services provided. Those surveys are of a number of customers who contacted Northern Powergrid regarding an unplanned or a planned power cut, requested a price quotation and a subsequent connection or had a general enquiry where a service had been provided or a job completed. In that respect, Northern Powergrid recorded an overall satisfaction score of 84.1% (2015: 81.9%) for the Regulatory Year.

Indicative of the continued, gradual improvement in the standard of customer service provided in the first half of 2016 was the achievement in May of an overall satisfaction score of 93.8% in respect of planned power cuts, which was the highest monthly score ever recorded in that category by any group of DNOs. The best ever overall customer satisfaction result was recorded in May 2016 but a slightly reduced score in June 2016 placed Northern Powergrid and its affiliate, Northern Powergrid (Yorkshire) plc, joint fourth in the ranking of DNOs, although only 0.2% separated the scores of the DNOs in joint fourth and second position. Individual performance in respect of power cuts, connections and general enquiries has been encouraging year-to-date and provides a solid base as further improvement initiatives are introduced.

Northern Powergrid continued to deliver its customer satisfaction improvement programme in respect of new connections to the network in the first half of 2016, which is focussed on actions derived from customers' feedback obtained from the weekly telephone surveys and is designed to support Northern Powergrid's goal to be the leading provider of customer service within the electricity distribution sector.

Operational excellence

Northern Powergrid continued to implement its approved network investment strategy in order to deliver improvements in an efficient and cost-effective manner and to enhance the distribution network's resilience and invested £90.4 million in the network during the six months to 30 June 2016, which was a decrease on the £116.7 million recorded in the six months to 30 June 2015 and included the refurbishment, replacement and construction of assets such as substations, transformers, switchgear and overhead and underground cables so that the number of power cuts that occur and number of customers affected by those power cuts are minimised as far as possible. That investment and the locally-focussed basis of Northern Powergrid's operations have contributed to average high-voltage and low-voltage restoration times being in line with their year-to-date targets.

Northern Powergrid responded well to the high winds that impacted its network during Storm Gertrude on 29 January 2016, which resulted in Northern Powergrid invoking its major incident management plan. 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.

INTERIM MANAGEMENT REPORT (CONTINUED)

Operational excellence (continued)

IUS continued to operate its engineering contracting business and saw a reduction in revenues in the six months to 30 June 2016, mainly due to lower activity in delivering contracts for Network Rail. Work on private electrical infrastructure for network owners in the North East of England and Yorkshire and on Multi-Utility contracts, which relate to the provision of electric, gas and water connections to housing developers, has increased in 2016. However, competition for business in the sectors, within which IUS operates, remained strong.

Metering continued to deliver a satisfactory performance in terms of the contracts secured with energy suppliers for the provision of smart meters in the United Kingdom and Ireland and also to develop further opportunities with other energy suppliers.

Employee commitment – Health and safety

The safety of its employees continued to be of paramount importance to the Group, with the on-going focus being on the goal 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. During the six months to 30 June 2016, the Group did not experience any lost time accidents (six months to 30 June 2015: Nil) against an annual target of one and incurred seven preventable vehicle accidents (six months to 30 June 2015: 4) against an annual target of 11.

The Group's continued use of targeted online driver training has assisted in reducing slow-speed and reversing incidents in the year to date and the exercise to equip all fleet vehicles with fully-operational telematics equipment was completed in May. The impact of this investment on accident rates will be subject to on-going assessment and accident investigations are able to utilise the technology in order to assist with identification of root causes and to support improvements in driving behaviour.

Environmental respect

Environmental performance for the first half of 2016 was encouraging with leakage rates from underground cables and oil-filled equipment continuing to be below historic levels over that part of the year and all of the Northern Powergrid Group's key performance indicators being ahead of target. That performance was supported by increased awareness of environmental matters across the Group'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.

In addition, Northern Powergrid was presented with a Silver award at the Zero Waste Awards 2016 for excellence in recycling and waste management, which recognise contributions made by businesses to create a more sustainable and resourceful economy by embedding waste reduction practices into their operations.

INTERIM MANAGEMENT REPORT (CONTINUED)

Principal risks and uncertainties

Regulatory risk

During the current price control period, which is known as ED1 and runs until 31 March 2023, the rate of inflation, as measured by the Retail Prices Index ("RPI"), is taken into account in setting Northern Powergrid's allowed income in respect of each regulatory year. Consequently, one of the risks faced by Northern Powergrid is that its costs may increase by more than RPI. Any changes in costs incurred will have a direct impact on Northern Powergrid's financial results, as will changes in performance under incentive schemes, such as in customer service, which can lead to adjustments to allowed revenues. In addition, the following are likely to have an impact on Northern Powergrid's financial performance during the ED1 period:

- the period over which new regulatory assets are depreciated is being gradually lengthened, from 20 years to 45 years;
- allowed revenues will be adjusted during the ED1 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 ED1 period by reference to a long-run trailing average based on external benchmarks of public debt costs; and
- 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.

Many aspects of the previous price control remain in place, including adjustments to revenues in relation to the number and duration of power cuts and customer service standards. There is also scope for a mid-period review and adjustment to revenues in the latter half of the ED1 period for any changes in the outputs required of licensees for certain specified reasons.

Financial risk

The principal risks associated with the regulatory environment, within which Northern Powergrid operates, are mentioned above.

As IUS' business is primarily in the competitive engineering contracting market, it continues to be subject to the issues created by the general economic environment and trading conditions and the associated fluctuations in demand for its services. In addition, there continues to be an enhanced risk of counter-party default, with the associated increase in the potential for IUS to be exposed to bad debt.

Northern Powergrid Metering operates as a meter asset provider, exposed to the risk of payment default, it reduces the risk by adhering to credit checking, payment terms, payment performance tracker and debt management, as a result its overdue debt position was not considered material.

The Group addresses interest rate risk by a policy of having a stable, low cost of financing over time, whilst observing approved risk parameters. The Group finances its activities by a combination of long-term borrowings at fixed rates of interest and by having access to short-term borrowing facilities at floating rates.

INTERIM MANAGEMENT REPORT (CONTINUED)

Principal risks and uncertainties (continued)

Financial risk (continued)

As at 30 June 2016, 100% of the Group's long-term borrowings were at fixed rates and the average maturity for these borrowings was 12 years. No material currency risks are faced by the Group and it is policy that no trading in financial instruments should be undertaken.

Northern Powergrid operates a stable and regulated business, in respect of which its allowed income is set in respect of each regulatory year through the special conditions in the electricity distribution licence. The principal risk is of an increase to the deficit currently attributable to the defined benefit pension scheme, of which the Company is the Principal Employer, given current volatility and uncertainty in the financial markets. The triennial valuation as at 31 March 2016 is currently ongoing, as part of which the Group and the Trustees will agree contributions required (if any) to ensure the scheme is fully funded over time on the basis of suitable, prudent assumptions.

Further information on the principal long-term risks and uncertainties and the internal control system are included in the Group's latest annual reports and accounts for the year to 31 December 2015, which is available at www.northernpowergrid.com.

It is anticipated that these risks will continue for the remaining six months of 2016.

Going concern

In the Group's latest annual reports and accounts for the year to 31 December 2015 the directors set out a number of factors they took into account when they considered continuing to adopt the going concern basis in preparing those annual reports and accounts. The directors confirm that no events have occurred during the six months to 30 June 2016, which alter the view expressed in the annual reports and accounts to 31 December 2015.

Future strategy and objectives

The Company will continue to develop its business as a holding company in a manner that concentrates on the Group's principal activities of electricity distribution, engineering contracting and the rental of meters to energy suppliers.

Northern Powergrid will continue to develop its business by operating with the goal of efficiently investing in the distribution network and improving the quality of supply and service provided to customers and delivering the regulatory business plan for ED1.

IUS will look to develop further its engineering contracting business by delivering a high standard of service to its existing clients and pursuing further opportunities in other sectors.

Metering will continue to explore commercial opportunities to develop its business in smart metering sector.

INTERIM MANAGEMENT REPORT (CONTINUED)

Responsibility Statement

The board of directors confirm that to the best of their knowledge:

- (a) the condensed set of financial statements, which has been prepared in accordance with IAS 34, "Interim Financial Reporting", gives a true and fair view of the assets, liabilities, financial position and profit of the Company and the undertakings included in the consolidation as a whole as required by DTR 4.2.4 R for the six months to 30 June 2016;
- (b) the interim management report contains a fair review of the information required by DTR 4.2.7 R (indication of important events during the first six months of the year and description of the principal risks and uncertainties for the remaining six months of the year); and
- (c) the interim management report includes a fair review of the information required by DTR 4.2.8 R (related parties' transactions and changes therein).

By order of the board

A handwritten signature in black ink, appearing to read 'T E Fielden', with a stylized flourish at the end.

T E Fielden
Director

23 September 2016

CONDENSED FINANCIAL STATEMENTS – SIX MONTHS ENDED 30 JUNE 2016

CONDENSED CONSOLIDATED STATEMENT OF PROFIT OR LOSS - SIX MONTHS ENDED 30 JUNE 2016

	6 Months ended 30 June 2016 (unaudited) £m	6 Months ended 30 June 2015 (unaudited) £m
Revenue	190.0	200.6
Cost of sales	<u>(20.4)</u>	<u>(22.1)</u>
Gross profit	169.6	178.5
Operating expenses	<u>(75.8)</u>	<u>(71.3)</u>
Operating profit	93.8	107.2
Other gains	0.4	0.2
Finance income	0.2	0.8
Finance costs	<u>(19.4)</u>	<u>(18.2)</u>
Profit before tax	75.0	90.0
Income tax expense	<u>(15.4)</u>	<u>(19.3)</u>
Profit from ordinary activities after tax	<u>59.6</u>	<u>70.7</u>

CONDENSED FINANCIAL STATEMENTS – SIX MONTHS ENDED 30 JUNE 2016

CONDENSED CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME - SIX MONTHS ENDED 30 JUNE 2016

	6 Months ended 30 June 2016 (unaudited) £m	6 Months ended 30 June 2015 (unaudited) £m
PROFIT FOR THE PERIOD	59.6	70.7
OTHER COMPREHENSIVE INCOME		
Items that will not be reclassified subsequently to profit or loss:		
Employee benefit obligation	15.8	(15.0)
Income tax relating to items of other comprehensive income	<u>(2.9)</u>	<u>3.0</u>
OTHER COMPREHENSIVE INCOME FOR THE YEAR, NET OF INCOME TAX	<u>12.9</u>	<u>(12.0)</u>
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	<u>72.5</u>	<u>72.5</u>

CONDENSED FINANCIAL STATEMENTS – SIX MONTHS ENDED 30 JUNE 2016

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION - SIX MONTHS ENDED 30 JUNE 2016

	30 June 2016 (unaudited) £m	31 December 2015 £m
ASSETS		
NON-CURRENT ASSETS		
Intangible assets	36.2	31.6
Property, plant and equipment	2,228.6	2,130.1
Investments	3.8	3.5
Pension asset	119.8	88.1
Trade and other receivables	9.5	8.8
	<u>2,398.0</u>	<u>2,262.2</u>
CURRENT ASSETS		
Inventories	11.9	13.5
Trade and other receivables	75.5	73.8
Cash and cash equivalents	-	8.8
	<u>87.4</u>	<u>96.1</u>
TOTAL ASSETS	<u>2,485.4</u>	<u>2,358.3</u>
EQUITY		
SHAREHOLDERS' EQUITY		
Share capital	72.2	72.2
Share premium account	158.8	158.8
Other reserves	6.2	6.2
Retained earnings	844.0	771.5
TOTAL EQUITY	<u>1,081.2</u>	<u>1,008.7</u>

CONDENSED FINANCIAL STATEMENTS – SIX MONTHS ENDED 30 JUNE 2016

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION - SIX MONTHS ENDED 30 JUNE 2016

	30 June 2016 (unaudited) £m	31 December 2015 £m
LIABILITIES		
NON-CURRENT LIABILITIES		
Trade and other payables	544.3	526.8
Borrowings	487.2	487.2
Deferred tax	108.8	104.9
Provisions	1.2	2.0
	<u>1,141.5</u>	<u>1,120.9</u>
CURRENT LIABILITIES		
Trade and other payables	125.1	110.1
Borrowings	132.2	113.6
Tax payable	3.6	4.0
Provisions	1.8	1.0
	<u>262.7</u>	<u>228.7</u>
TOTAL LIABILITIES	<u>1,404.2</u>	<u>1,349.6</u>
TOTAL EQUITY AND LIABILITIES	<u>2,485.4</u>	<u>2,358.3</u>

The interim financial statements were approved by the board of directors and authorised for issue on 23 September 2016 and were signed on its behalf by:



T E Fielden
Director

CONDENSED FINANCIAL STATEMENTS – SIX MONTHS ENDED 30 JUNE 2015

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY - SIX MONTHS ENDED 30 JUNE 2016

	Share Capital £m	Share Premium Account £m	Other Reserves £m	Retained Earnings £m	Total £m
Balance at 1 January 2016	72.2	158.8	6.2	771.5	1,008.7
Profit for the period (unaudited)	-	-	-	59.6	59.6
Other comprehensive income (unaudited)	-	-	-	12.9	12.9
Balance at 30 June 2016	<u>72.2</u>	<u>158.8</u>	<u>6.2</u>	<u>844.0</u>	<u>1,081.2</u>

	Share Capital £m	Share Premium Account £m	Other Reserves £m	Retained Earnings £m	Total £m
Balance at 1 January 2015	72.2	158.8	6.2	649.7	886.9
Profit for the period (unaudited)	-	-	-	70.7	70.7
Other comprehensive income (unaudited)	-	-	-	(12.0)	(12.0)
Balance at 30 June 2015	<u>72.2</u>	<u>158.8</u>	<u>6.2</u>	<u>708.4</u>	<u>945.6</u>

	Share Capital £m	Share Premium Account £m	Other Reserves £m	Retained Earnings £m	Total £m
Balance at 1 January 2015	72.2	158.8	6.2	649.7	886.9
Profit for the year	-	-	-	144.9	144.9
Other comprehensive income	-	-	-	(2.5)	(2.5)
Dividends	-	-	-	(20.6)	(20.6)
Balance at 31 December 2015	<u>72.2</u>	<u>158.8</u>	<u>6.2</u>	<u>771.5</u>	<u>1,008.7</u>

CONDENSED FINANCIAL STATEMENTS – SIX MONTHS ENDED 30 JUNE 2016

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

	6 Months ended 30 June 2016 (unaudited) £m	6 Months ended 30 June 2015 (unaudited) £m
Cash generated from operations	108.3	113.6
Net interest paid	(17.8)	(18.1)
Tax paid	(14.7)	(12.2)
Net cash from operating activities	<u>75.8</u>	<u>83.3</u>
Investing activities		
Proceeds from disposal of property, plant and equipment	0.2	0.2
Purchase of property, plant and equipment	(120.6)	(148.0)
Purchase of intangible assets	(6.1)	(5.2)
Dividends received from joint venture	-	0.5
Receipt of customer contributions	26.1	20.9
Net cash used in investing activities	<u>(100.4)</u>	<u>(131.6)</u>
Financing activities		
Movement in external loans	12.4	(9.0)
Movement in loans from group undertakings	3.4	-
Net cash generated/(used in) by financing activities	<u>15.8</u>	<u>(9.0)</u>
Net decrease in cash and cash equivalents	(8.8)	(57.3)
Cash and cash equivalents at beginning of period	<u>8.8</u>	<u>85.6</u>
Cash and cash equivalents at end of period	<u>-</u>	<u>28.3</u>

NOTES TO THE CONDENSED FINANCIAL STATEMENTS

1. GENERAL INFORMATION

The information included within these condensed financial statements for the year ended 31 December 2015, does not constitute statutory accounts as defined in section 434 of the Companies Act 2006. A copy of the statutory accounts for that year has been delivered to the Registrar of Companies. The auditor reported on those accounts and that report was unqualified, did not draw attention to any matters by way of emphasis and did not contain a statement under section 498(2) or (3) of the Companies Act 2006.

2. ACCOUNTING POLICIES

Basis of preparation

The annual financial statements of the Group are prepared in accordance with International Financial Reporting Standards as adopted by the European Union. The condensed set of financial statements included in this half-yearly financial report has been prepared in accordance with International Accounting Standard 34, 'Interim Financial Reporting', as adopted by the European Union.

Going concern

In the Company's latest annual reports and accounts for the year to 31 December 2015 the directors set out a number of factors they took into account when they considered continuing to adopt the going concern basis in preparing those annual reports and accounts. The directors confirm that no events have occurred during the six months to 30 June 2016, which alter the view expressed in the annual reports and accounts to 31 December 2015.

Changes in accounting policy

The Group's accounting policies and methods of computation are the same as the accounting policies which are described in the Group's financial statements for the year ended 31 December 2015. The Group has not adopted any new or revised accounting standards in the current year.

CONDENSED FINANCIAL STATEMENTS - SIX MONTHS ENDED 30 JUNE 2016

NOTES TO THE CONDENSED FINANCIAL STATEMENTS (CONTINUED)

3. SEGMENTAL ANALYSIS

The Group operates in the principal area of activity of the distribution of electricity in the United Kingdom.

There has been no change in the basis of segmentation or in the basis of measurement of segment profit or loss in the period.

The following is an analysis of the Group's revenue and results by reportable segment in the six months ended 30 June 2016 (unaudited):

	Distribution £m	Contracting £m	Other £m	Consolidation Adjustments £m	Total £m
REVENUE					
External sales	165.3	14.5	10.2	-	190.0
Inter-segment sales	0.3	0.9	(0.3)	(0.9)	-
Total Revenue	165.5	15.4	9.9	(0.9)	190.0
SEGMENT RESULTS					
Operating profit	77.0	0.1	1.1	15.6	93.8
Other gains					0.4
Finance income					0.2
Finance costs					(19.4)
Profit before tax					75.0
OTHER INFORMATION					
Capital additions	99.1	-	26.6	-	142.9
Depreciation and amortisation	37.9	-	4.4	(0.9)	41.4
Amortisation of deferred revenue	9.4	-	-	-	9.4

CONDENSED FINANCIAL STATEMENTS - SIX MONTHS ENDED 30 JUNE 2016

NOTES TO THE CONDENSED FINANCIAL STATEMENTS (CONTINUED)

3. SEGMENTAL ANALYSIS (CONTINUED)

The following is an analysis of the Group's revenue and results by reportable segment in the six months ended 30 June 2015 (unaudited):

	Distribution £m	Contracting £m	Other £m	Consolidation Adjustments £m	Total £m
REVENUE					
External sales	178.8	16.0	5.8	-	200.6
Inter-segment sales	0.3	1.4	(0.2)	(1.5)	-
Total Revenue	<u>179.1</u>	<u>17.4</u>	<u>5.6</u>	<u>(1.5)</u>	<u>200.6</u>
SEGMENT RESULTS					
Operating profit	<u>90.4</u>	<u>0.2</u>	<u>(0.4)</u>	<u>17.0</u>	107.2
Other gains					0.2
Finance income					0.8
Finance costs					<u>(18.2)</u>
Profit before tax					<u>90.0</u>
OTHER INFORMATION					
Capital additions	116.8	-	26.6	-	143.4
Depreciation and amortisation	35.8	-	1.3	(0.9)	36.2
Amortisation of deferred revenue	<u>10.4</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>10.4</u>

"Other" comprises smart meter rental and business support units.

Sales and purchases between the different segments are made at commercial prices.

External sales to RWE Npower plc in the six months ended 30 June 2016 of £40.1 million (30 June 2015: £48.2 million) are included within the Distribution segment.

External sales to British Gas Ltd in the six months ended 30 June 2016 of £20.4 million (30 June 2015: £22.7 million) are included within the Distribution segment.

CONDENSED FINANCIAL STATEMENTS - SIX MONTHS ENDED 30 JUNE 2016

NOTES TO THE CONDENSED FINANCIAL STATEMENTS (CONTINUED)

3. SEGMENTAL ANALYSIS (CONTINUED)

The accounting policies of the reportable segments are the same as the Group's accounting policies which are described in the Group's latest annual financial statements. The segment results represent the profit earned by each segment without allocation of the share of profits of joint ventures, associates, finance income and finance costs and income tax expense.

Segment net assets	30 June 2016 Unaudited £m	31 December 2015 £m
Distribution	1,620.3	1,576.1
Contracting	12.8	11.4
Other	107.8	74.1
Consolidation Adjustments	<u>(52.1)</u>	<u>44.4</u>
Total net assets by segment	1,688.7	1,706.0
Unallocated net corporate liabilities	<u>(607.5)</u>	<u>(697.5)</u>
Total net assets	<u><u>1,081.2</u></u>	<u><u>1,008.5</u></u>

Unallocated net corporate liabilities include cash and cash equivalents of £nil million (December 2015: £8.8 million), borrowings of £618.9 million (December 2015: £601.1 million), retirement benefit asset of £119.8 million (December 2015: £88.1 million), and taxation of £112.4 million (December 2015: £108.8 million).

CONDENSED FINANCIAL STATEMENTS - SIX MONTHS ENDED 30 JUNE 2016

NOTES TO THE CONDENSED FINANCIAL STATEMENTS (CONTINUED)

4. INCOME TAX EXPENSE

Tax for the six month period ended 30 June 2016 is charged at 20.00% (six months ended 30 June 2015: 20.25%; year ended 31 December 2015: 20.25%) which represents the best estimate of the average annual effective tax rate expected for the full year, as applied to the pre-tax income of the six month period.

	6 months ended 30 June 2015 Unaudited £m	6 months ended 30 June 2014 Unaudited £m
Current tax	11.7	13.7
Deferred tax	<u>3.7</u>	<u>5.6</u>
Total income tax expense	<u>15.4</u>	<u>19.3</u>

The Finance No 2 Act 2015 included a provision that the standard rate of corporation tax in the United Kingdom was to reduce from 20% to 19% from April 2017 and to 18% from April 2020. Deferred taxation is measured at the tax rates that apply in the periods in which the temporary differences are expected to reverse based on the tax rates and laws that have been substantively enacted at the statement of financial position date. Accordingly, 18% has been applied when calculating deferred tax assets and liabilities as at 30 June 2016.

The Finance Bill 2016 contains provisions to further reduce the rate of corporation tax to 17% with effect from 1 April 2020. It is expected that the Finance Act 2016 will be substantively enacted in October 2016. As substantive enactment of Finance Act 2016 is after the statement of financial position date the further reduction to the rate of UK corporation tax has been disregarded in calculating the deferred tax position at 30 June 2016.

CONDENSED FINANCIAL STATEMENTS - SIX MONTHS ENDED 30 JUNE 2016

NOTES TO THE CONDENSED FINANCIAL STATEMENTS (CONTINUED)

5. NOTES TO THE CASH FLOW STATEMENT

	6 Months ended 30 June 2016 (unaudited) £m	6 Months ended 30 June 2015 (unaudited) £m
Profit before income tax	75.0	90.0
Depreciation charges	41.4	36.2
Profit on disposal of fixed assets	(0.2)	(0.2)
Amortisation of deferred revenue	(9.5)	(10.4)
Retirement benefit obligations	(15.9)	(18.0)
Decrease in provisions	(0.2)	(0.6)
Finance costs	19.4	18.2
Finance income	(0.2)	(0.8)
	<u>109.8</u>	<u>114.4</u>
Decrease/(increase) in inventories	1.5	(1.2)
(Increase)/decrease in trade and other receivables	(2.1)	5.6
(Decrease) in trade and other payables	(0.9)	(4.2)
	<u>108.3</u>	<u>113.6</u>
Cash generated from operations	<u>108.3</u>	<u>113.6</u>

6. RETIREMENT BENEFIT SCHEMES

The defined benefit obligation as at 30 June 2016 is calculated on a year-to-date basis, using the annual actuarial valuation as at 31 December 2015. If the current market conditions as at 30 June 2016 were to be adopted, the amount recognised pre-tax in Other Comprehensive Income would be £247.4m and the pension expense for the year ended 31 December 2016 would increase by £1.1 to £13.6m. However due to the current volatility of the market the interim accounts have not been adjusted and the 2016 annual reports and accounts will reflect market conditions as at 31 December 2016.

CONDENSED FINANCIAL STATEMENTS - SIX MONTHS ENDED 30 JUNE 2016

NOTES TO THE CONDENSED FINANCIAL STATEMENTS (CONTINUED)

7. FINANCIAL INSTRUMENTS

Except as detailed in the following table, the directors consider that the carrying value amounts of financial assets and financial liabilities are approximately equal to their fair values:

	Carrying value		Fair value	
	30 June 2016 Unaudited £m	31 December 2015 £m	30 June 2016 Unaudited £m	31 December 2015 £m
Financial liabilities				
Inter-company short-term loan	3.4	0.2	3.4	0.2
Bond 2020 – 8.875% (Northern Electric Finance plc)	105.6	101.1	136.7	130.6
Bond 2035 – 5.125% (Northern Electric Finance plc)	149.1	152.9	197.6	180.5
EIB Loan (2018-2020)*	120.4	123.4	131.4	132.8
EIB Loan 2027 – 2.564% (Northern Powergrid (Northeast) Ltd Yorkshire Electricity Group plc 2037 – 5.9%)	121.7	120.1	130.9	117.1
	102.9	100.0	145.8	132.1
Cumulative preference shares	3.4	3.4	167.5	160.8
	<u>542.9</u>	<u>552.2</u>	<u>913.3</u>	<u>854.1</u>

* The borrowings from the European Investment Bank were drawn down in twelve tranches, repayable in 2018, 2019 and 2020. The spread of interest rate is as follows:

2018: 3.901% - 4.283%

2019: 4.077% - 4.455%

2020: 4.227% - 4.586%

CONDENSED FINANCIAL STATEMENTS - SIX MONTHS ENDED 30 JUNE 2016

NOTES TO THE CONDENSED FINANCIAL STATEMENTS (CONTINUED)

8. RELATED PARTY TRANSACTIONS

Group

Transactions entered into with related parties and balances outstanding were as follows:

	Sales to related parties £m	Purchases from related parties £m	Amounts owed to related parties £m	Borrowings from related parties £m	Finance income/ (costs) from/(to) related parties £m
Related party					
<i>Six months ended 30 June</i>					
<i>2016:</i>					
Northern Powergrid Limited	-	-	-	-	(3.1)
Northern Powergrid (Yorkshire) plc	8.4	4.9	-	-	-
Vehicle Lease and Service Limited	0.1	2.2	0.4	-	0.4
Yorkshire Electricity Group plc	-	-	-	102.9	(3.2)
	<u>8.5</u>	<u>7.4</u>	<u>0.3</u>	<u>102.9</u>	<u>(5.9)</u>
<i>Six months ended 30 June</i>					
<i>2015:</i>					
Northern Powergrid Gas Limited	0.1	-	-	-	-
Northern Powergrid Insurance Services Limited	-	0.2	-	-	-
Northern Powergrid Limited	-	-	-	-	(3.1)
Northern Powergrid (Yorkshire) plc	9.8	4.5	-	-	-
Vehicle Lease and Service Limited	0.1	2.0	0.3	0.6	0.4
Yorkshire Electricity Group plc	-	-	-	102.9	(2.9)
	<u>10.0</u>	<u>6.7</u>	<u>0.3</u>	<u>103.5</u>	<u>(5.6)</u>

CONDENSED FINANCIAL STATEMENTS - SIX MONTHS ENDED 30 JUNE 2016

NOTES TO THE CONDENSED FINANCIAL STATEMENTS (CONTINUED)

8. RELATED PARTY TRANSACTIONS (CONTINUED)

Group - continued

	Sales to related parties £m	Purchases from related parties £m	Amounts owed to related parties £m	Borrowings to/(from) related parties £m	Finance income/ (costs) from/(to) related parties £m
Related party					
<i>Year ended 31 December</i>					
<i>2015:</i>					
Integrated Utility Services Limited (registered in Eire)	-	2.8	0.1	-	-
Northern Powergrid Gas Limited	0.1	-	-	-	-
Northern Powergrid Insurance Services Limited	-	0.3	-	-	-
Northern Powergrid Limited	-	-	-	-	(6.2)
Northern Powergrid (Yorkshire) plc	25.7	10.7	-	-	-
Vehicle Lease and Service Limited	0.2	3.7	0.4	-	0.6
Yorkshire Electricity Group plc	-	-	-	100.2	(6.0)
	<u>26.0</u>	<u>17.5</u>	<u>0.5</u>	<u>100.2</u>	<u>(11.6)</u>

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

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

During the six months ended 30 June 2016 two directors (six months ended 30 June 2015: 2, year ended 31 December 2015: 2) utilised the services provided by Northern Transport Finance Limited, a subsidiary company.

CONDENSED FINANCIAL STATEMENTS - SIX MONTHS ENDED 30 JUNE 2016

NOTES TO THE CONDENSED FINANCIAL STATEMENTS (CONTINUED)

8. RELATED PARTY TRANSACTIONS (CONTINUED)

Company

Transactions entered into with related parties and balances outstanding were as follows:

	Sales to related parties £m	Purchases from related parties £m	Borrowings to/(from) related parties £m	Finance income/ (costs) from/(to) related parties £m
Related party				
<i>Six months ended 30 June 2016:</i>				
Integrated Utility Services Limited	-	0.3	-	-
Northern Powergrid Gas Limited	0.1	-	-	-
Northern Powergrid Limited	-	-	-	(3.1)
Northern Powergrid (Northeast) Limited	3.2	-	-	-
Northern Powergrid (Yorkshire) plc	2.5	-	-	-
Vehicle Lease and Service Limited	0.1	-	-	-
Yorkshire Electricity Group plc	-	-	27.0	-
	<u>5.9</u>	<u>0.3</u>	<u>27.0</u>	<u>(3.1)</u>
<i>Six months ended 30 June 2015:</i>				
Integrated Utility Services Limited	-	0.3	-	-
Northern Powergrid Gas Limited	0.1	-	-	-
Northern Powergrid Limited	-	-	-	(3.1)
Northern Powergrid (Northeast) Limited	3.7	-	-	-
Northern Powergrid (Yorkshire) plc	2.3	-	-	-
Vehicle Lease and Service Limited	0.1	-	-	0.4
Yorkshire Electricity Group plc	-	-	29.0	0.1
	<u>6.2</u>	<u>0.3</u>	<u>29.0</u>	<u>(2.6)</u>

CONDENSED FINANCIAL STATEMENTS - SIX MONTHS ENDED 30 JUNE 2016

NOTES TO THE CONDENSED FINANCIAL STATEMENTS (CONTINUED)

8. RELATED PARTY TRANSACTIONS (CONTINUED)

Company – continued

	Sales to related parties £m	Purchases from related parties £m	Amounts owed to related parties £m	Borrowings to/(from) related parties £m	Finance income/ (costs) from/(to) related parties £m
Related party					
<i>Year ended 31 December</i>					
<i>2015:</i>					
Integrated Utility Services Limited	0.1	0.5	-	-	-
Northern Powergrid Gas Limited	0.1	-	-	-	-
Northern Powergrid Limited	-	-	-	-	(6.2)
Northern Powergrid (Northeast) Limited	6.4	0.1	-	-	20.6
Northern Powergrid (Yorkshire) plc	4.0	-	-	-	-
Vehicle Lease and Service Limited	0.2	-	-	-	0.5
Yorkshire Electricity Group plc	-	-	-	24.3	0.2
	<u>10.8</u>	<u>0.6</u>	<u>-</u>	<u>24.3</u>	<u>15.1</u>

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

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