

NORTHERN ELECTRIC DISTRIBUTION LIMITED

REGISTERED NUMBER 2906593

**REPORT & ACCOUNTS
TO 31 DECEMBER 2008**

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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REPORT AND ACCOUNTS TO 31 DECEMBER 2008

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NORTHERN ELECTRIC DISTRIBUTION LIMITED

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

DIRECTORS' REPORT

Cautionary statement regarding forward-looking statements

This annual report has been prepared for the members of the Company only. The Company, its directors, employees or agents do not accept or assume responsibility to any other person in connection with this document and any such responsibility or liability is expressly disclaimed. This annual report contains 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 this annual report, and will not be updated during the year. Nothing in this annual report should be construed as a profit forecast.

The directors present the annual report and accounts of Northern Electric Distribution Limited (the "Company") for the year ended 31 December 2008, which includes the business review and audited financial statements for that year. Pages 1 to 18 inclusive of this annual report comprise a directors' report that has been drawn up and presented in accordance with the Companies Act 1985.

PRINCIPAL ACTIVITIES

The Company is part of the CE Electric UK Funding Company group of companies (the "CE Group") and its principal activity during the year was to distribute electricity to customers connected to its electricity distribution network.

The Company serves an area of approximately 14,400 sq km in the north east of England with a resident population of 3.2 million, receives electricity from the National Grid's transmission system and distributes it to the 1.6 million customers connected to its electricity distribution network of transformers, switchgear and overhead and underground cables, at voltages of up to 132kV. The Company is an authorised distributor under the Electricity Act 1989 and holds an electricity distribution licence granted by the Secretary of State. During the year, the Company distributed electricity to customers in its distribution services area and continued to improve the overall performance of its distribution network through its investment strategy being targeted at delivering improvements in an efficient and cost-effective manner.

In common with the CE Group, the Company operates a business model and strategy based on its six core principles, which are:

<u>Principle</u>	<u>Strategy</u>	<u>Indicator</u>
Financial strength	Effective stewardship of the Company's financial resources and investing in assets and focusing on long term opportunities, which contribute to the Company's future strength.	Profitability. Cash flow. Maintenance of investment grade credit ratings.
Customer service	Delivering reliability, fair prices and exceptional service.	Improving network resilience and performance, measured by: Customer minutes lost; Customer interruptions; and Customer satisfaction.

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DIRECTORS' REPORT (CONTINUED)

PRINCIPAL ACTIVITIES (continued)

Operational excellence	Setting high standards for the Company's operations and system investment, operation and maintenance.	Effective asset management. Managing commercial risk. Improving network resilience and performance.
Employee commitment	Equipping employees with the resources and skills they need to operate successfully and in a safe and rewarding environment.	Leading safety performer. Engaging employees. Effective leadership.
Environmental respect	Using natural resources wisely and effectively protecting the environment, where it is impacted by the Company's operations.	Reducing environmental impact. Promoting and pursuing long term sustainability.
Regulatory integrity	Adhering to a policy of strict compliance with appropriate standards, policies and legislation.	Strong internal controls. Regulatory engagement. Industry influence.

The Company continually puts plans in place to deliver its objectives against the strategy based on its core principles. The Company executes on those plans across a range of activities, measures its progress against those plans and introduces corrective action wherever required. Adherence to its strategy and core principles enabled the Company to deliver a high standard of performance against the challenges faced during 2008.

BUSINESS REVIEW

Review of the year

The Company's progress during the year was pleasing, with the highlights being a strong underlying financial performance, improved customer service performance in the call centre and a significant improvement in the lead times for producing high volume quotations for connections to the distribution network. There were also general reductions in accident rates, oil leakages from fluid-filled cables and guaranteed standards of performance failures. These highlights were achieved while managing a sustained period of industrial action.

Issues identified as being central to delivery of the core principles in the future include further improvements in safety performance, network availability and reliability and the usefulness and accuracy of information provided to customers during network outages. In addition, the process of negotiating Distribution Price Control Review 5 ("DPCR5") will be a critical area of focus during 2009 as the outcome will set the Company's income through to March 2015.

Strategic objectives

As part of the CE Group, the Company's strategic objectives, based on its core principles, are to build a business, which

- continues to generate value over the long-term, in keeping with the nature of that business;
- invests in and manages its electricity distribution network in an efficient and effective manner;

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DIRECTORS' REPORT (CONTINUED)

Strategic objectives (continued)

- 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 terms of shaping the future direction of the electricity distribution network sector in the United Kingdom.

As part of its strategy, the Company is committed to putting safety first, respecting its customers, their time and property, doing a quality job, responding effectively in times of severe weather (when it is needed most) and caring for its local environment.

Principal risks and uncertainties

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

Financial strength:

The main financial risks facing the Company are outlined in the Treasury section on page 8 below.

As a holder of an electricity distribution licence, the Company is subject to regulation by the Gas and Electricity Markets Authority, which acts through the Office of Gas and Electricity Markets ("Ofgem").

Most of the revenue of the electricity distribution licence holders is controlled by a distribution price control formula set out in the electricity distribution licence. The price control formula does not constrain profits from year to year but is a control on revenue that operates independently of most of the electricity distribution licence holder's costs.

It has been the practice of Ofgem to review and reset the formula at five-year intervals, although the formula has been, and may be, reviewed at other times at the discretion of Ofgem. The current five-year price control period became effective on 1 April 2005 and has set the Company's revenue through to 31 March 2010. A resetting of the formula requires the consent of the electricity distribution licence holder but licence modifications may be unilaterally imposed by Ofgem without such consent following review by the Competition Commission. During the term of the price control, changes in costs incurred will have a direct impact on the financial results of the Company.

During 2009, the Company will be fully engaged with Ofgem in the DPCR5 process, which will culminate in Ofgem making its final proposals in respect of the price control formula that will take effect for the five-year period commencing 1 April 2010. That process involved submission of the Company's detailed business plans in February 2009, triggering an assessment by Ofgem that will result in an initial set of proposals to be published in mid-2009. Dialogue between the Company and Ofgem will take place throughout the second half of 2009 such that the final proposals are then expected prior to the end of the year.

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DIRECTORS' REPORT (CONTINUED)

Principal risks and uncertainties (continued)

Other:

The principal risks facing the Company in respect of the other core principles include:

<u>Risk</u>	<u>Issue</u>	<u>Mitigation</u>
Counter-party security	A counter-party with which the Company trades may go bankrupt causing loss of invested funds or amounts owing.	The treasury function has strict controls in respect of the counter-parties with which it deals, including the use of credit ratings and appropriate limits. Credit cover arrangements are in place with the electricity suppliers, which would allow recovery of defaulted payments through the price control mechanism, if good debt control practices continue to be followed.
Potential flooding and other weather related events.	Recent weather patterns suggest a heightened risk of flooding of 'at risk areas' and the potential for increased occurrence of damage to the overhead network.	A robust major incident management plan is in place. The Company's critical property unit plan assesses those properties most at risk and a flood mitigation plan is in place, including the erection of permanent and temporary defences.
Supply chain interfaces	The various operational areas of the Company may overlap or have gaps in the supply chain. Current economic conditions are placing suppliers under pressure.	Roles and responsibilities of the interfacing departments are being better defined. Payment for goods and services provided is within agreed terms, after due scrutiny.
BT ESP analogue circuits	Potential withdrawal of service puts existing communication arrangements at risk.	Options include retaining the equivalent service, potentially at higher than current cost or utilising an alternative solution.
Network risk posed by cables through the Tyne Tunnel	The 66kV fluid-filled cables in the tunnel are aging with increased risk of failure, leading to a requirement for the substantial use of generating units and potential guaranteed standards failures and incentive penalties.	The Company's Primary Engineering Projects team is developing a solution but has assessed the potential for simultaneously losing all circuits as being remote.
Motor accident management	Any significant road traffic accident involving a Company vehicle may create a liability, which the Company has to meet, and involve injury to employees and/or third parties.	The Safety Improvement Plan has a substantial focus on road risk and the reduction of preventable vehicle accidents. A dedicated road risk manager has been appointed.

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DIRECTORS' REPORT (CONTINUED)

Principal risks and uncertainties (continued)

Other (continued):

Electricity, Safety, Quality and Continuity Regulations 2002	The regulations impose various statutory obligations, non-compliance with which could lead to incidents, prosecution and claims.	A full site inspection and risk assessment regime is in place designed to ensure compliance.
Shortage of supply and increased demand for copper	The global demand for copper has impacted the availability and cost of a number of core products and increased the risk of theft.	Improved and more efficient procurement processes have been introduced and security at all sites where copper products are stored has been reviewed and enhanced where required.

A Compliance Assurance Programme Steering Group ("CAPSG") is in place, consisting of certain directors and senior managers of the CE Group in order to provide oversight at a strategic level and steering of the CE Group's performance in respect of governance and its key facets of compliance and risk management.

The Company operates a structured and disciplined approach to the management of risk, as part of the overall risk management approach of the CE Group. Those risks assessed to be significantly high are logged within a risk register that is reviewed regularly by the CAPSG and key indicators track the number of significant risks actively monitored by the CAPSG at any one time.

Risks are assessed with due regard to probability and impact and the risk environment is reviewed continually in order that new or emerging potential risks are identified. Risk mitigation and loss control plans are prepared in response to strategic risks in order that the directors can be assured that appropriate mitigating actions are in place and being implemented. These plans are monitored through to implementation and reviewed to determine whether the level of residual, mitigated risk is within an acceptable level of tolerance.

The CE Group's strategy is to follow an appropriate risk policy, which is intended to effectively manage exposures related to the achievement of business objectives. The CE Group identifies and assesses risks associated with the achievement of its strategic objectives, including those of an environmental and social nature. Any key actions needed to further enhance the control environment are identified, along with the person responsible for the management of the specific risk. A quarterly review of the key risks, controls and action plans is undertaken. The Governance and Risk Section oversees all aspects of risk and compliance, emphasising the CE Group's commitment to maintaining an appropriate risk and governance framework across the business.

The use of a well-defined risk management methodology allows a consistent and co-ordinated approach to risk reporting and mitigation.

A key element and requirement of the risk management process is that a written certificate is provided by the President and Chief Operating Officer of the CE 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 senior managers are required to confirm that the system of internal control in their area of the business is operating effectively.

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DIRECTORS' REPORT (CONTINUED)

Internal control

A rigorous internal control environment exists within the CE 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. MidAmerican Energy Holdings Company ("MidAmerican"), a parent company of the Company, requires a quarterly control risk self-assessment to be undertaken by all senior managers as part of its programme for compliance with the requirements of the Sarbanes-Oxley Act. During the year, an extensive programme to review the company-wide controls was completed and opportunities to enhance control arrangements, identified by that review, have been implemented.

The CE Group is committed to proper business conduct and, in common with the other affiliates of MidAmerican, has adopted a code of business ethics that emphasises the requirement for all staff to manage their activities to achieve the highest level of ethical conduct.

The CE Group has a "speaking up" policy in place for staff 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.

Human resource policies focus on skills, motivation and excellence and the promotion of high standards of probity among staff. In addition, the appropriate organisational structure has been developed to control business units and to delegate authority and accountability, having regard to acceptable levels of risk.

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. 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 to provide independent scrutiny of internal control systems and risk management procedures, including standards required by the Sarbanes-Oxley Act;
- On-going 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 the Occupational Health and Safety Assessment Series ("OHSAS") standard OHSAS 18001, which is subject to external certification and regular assessment;
- An external obligations programme, which provides a robust approach to, and compliance 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.

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DIRECTORS' REPORT (CONTINUED)

Financial strength

During 2008, the Company introduced improvements in its management of routine financial performance by identifying clearer lines of accountability, implementing tighter expenditure controls, improving management information and emphasising the culture of continuous financial improvement in all areas of operation.

In addition, representations were made to Ofgem, in accordance with the provisions set out in the electricity distribution licence, regarding certain categories of cost not fully taken into account when the current price control was set, effective from 1 April 2005, due to uncertainties at that time regarding the amount and materiality of those costs. After a due process of review Ofgem generally accepted those representations and agreed that the Company was able to recover approximately £18m, in addition to the otherwise agreed principles for calculating its allowed revenue, over the three regulatory years starting on 1 April 2009 and ending on 31 March 2012. The price control was adjusted accordingly.

The Company is keenly aware of the impact that the general economic climate is having, and may continue to have in the foreseeable future, on it and its customers. In that respect, procedures are in place to more closely monitor and manage the issues that may impact on the Company's business more significantly than others, including a reduction in overall demand for electricity leading to less units being distributed through the Company's network, lower activity in terms of new connections required to the network and the potential for higher debt write-off as the economic downturn further affects the Company's customers.

Key aspects of financial performance for the year were as follows:

Revenue

Revenue at £214.9m was £2.0m higher than the prior year as a result of increased deferred revenue amortisation and higher sales to affiliate companies.

Operating profit

Operating profit at £81.9m was £8.0m lower than the previous year, mainly due to an increase in pension deficit payments of £6.9m.

Finance costs

Finance costs at £24.1m were £1.5m higher than the prior year due to higher average net debt during the year.

Taxation

The Company's taxation charge in 2008 and 2007 has been affected by changes in tax rates and legislation. Details are provided in Note 8 to the accounts.

Results and dividends

The Company made a profit after tax for the year of £35.1m. An interim dividend of £20m was paid during the year and the directors recommend that no final dividend be paid in respect of the year.

Share capital and debt structures

There were no changes to the Company's share capital or debt structure during the year.

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DIRECTORS' REPORT (CONTINUED)

Financial strength (continued)

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 is remitted to Yorkshire Electricity Group plc ("YEG"), a fellow company in the CE 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 £73.3m was £13.7m lower than 2007, mainly due to higher pension deficit payments in the year (£6.9m) and adverse working capital movements (£6.1m).
- *Investing activities:* Net cash used in investing activities at £98.3m was broadly in line with the prior year and reflects the capital investment in the year offset by contributions made by customers to various projects.
- *Financing activities:* The net cash generated by financing activities at £30.2m was £15.6m higher than the prior year reflecting the increase in new borrowings in the year.

Treasury

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.

Liquidity risk

The Company has access to short-term borrowing facilities provided by YEG, £50m in committed revolving credit facilities provided by Lloyds TSB Bank plc and Royal Bank of Scotland plc and an additional overdraft facility of £2m provided by Lloyds TSB Bank plc, which is renewed on an annual basis. The revolving credit facilities are due to expire in April 2010, at which point, the Company expects to raise further facilities as required. The directors do not consider there to be any doubt over the Company's ability to raise such finance 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 December 2008, 79% of the Company's borrowings were at fixed rates and the average maturity for these borrowings was 24 years.

Currency risk

No material currency risks are faced by the Company.

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DIRECTORS' REPORT (CONTINUED)

Financial strength (continued)

Treasury (continued)

Trading risk

Throughout the year under review, the Company's policy was that no trading in financial instruments should be undertaken.

Financial derivatives

As at 31 December 2008 and during the year it was the Company's policy not to hold any derivative financial instruments.

Pensions

The Company is a participating company in the Northern Electric 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 accounts. The Company also participates in the Northern Electric Money Purchase Scheme, which is a defined contribution scheme.

Insurance

As part of its insurance and risk strategy, the CE Group has put in place a range of insurance policies covering it against risks, including damage to property and employer's, third party motor and public liability. The CE 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 year, the Company distributed electricity to customers in its distribution services area and continued to improve the overall performance of its distribution network through its investment strategy being targeted at delivering improvements in an efficient and cost-effective manner. The Company is focused on delivering a reliable and dependable supply of electricity and a high standard of service to its customers and, in the first full year of operation since the launch of the "customer promises", a significant number of tangible improvements have been identified and delivered, as part of the overall goal to improve customer satisfaction with the service provided, including:

- improving under-performing parts of the distribution system by identifying "hot spots" and taking specific action to address the issues in those areas;
- undertaking a programme to reduce the number of instances by one third, in which the Company fails to meet an electricity guaranteed standard of performance;
- advancing the community care programme for the most vulnerable customers by ensuring that the needs of those customers are understood and responded to as effectively as possible, making available dedicated customer support vehicles and providing a 'language line' to facilitate conversations between customers and staff; and
- taking action to reduce the average length of time taken to restore supplies in fault situations.

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DIRECTORS' REPORT (CONTINUED)

Customer service (continued)

The Company continued with its initiatives to reduce the time taken to restore supplies following faults on the network. Those initiatives include "Power in an Hour", which aims to restore the supplies of as many customers as possible within an hour of the start of an interruption, and the use of the latest mobile phone technology to locate and contact the nearest persons able to deal with faults.

The main achievements in 2008 were the overall reduction in failures against the guaranteed standards of performance, significant improvement in the quotation performance of the connections business and the naming of the customer relations centre as North East Contact Centre of the Year in its class. However, it is recognised that further effort is required to bring the Company's customer satisfaction scores to greater than 90% and the installation of a replacement telephone system that takes advantage of the latest developments in automatic messaging is expected to improve performance in this respect.

Ofgem has established an incentive scheme for quality of service, by which distribution network operators ("DNOs"), such as the Company, are provided with financial incentives based upon targets set by Ofgem for each of the DNOs with regard to their performance in the following areas:

- The number of interruptions to supply;
- The duration of interruptions to supply; and
- Customer satisfaction.

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 measure the average number of supply minutes lost for every connected customer due to faults and planned outages that last for three minutes or longer. CI measure the average number of supply interruptions for every 100 connected customers due to faults and planned outages that last for three minutes or longer. DNOs' performance against guaranteed standards, set for activities such as restoring supplies after unplanned interruptions, provides a measure of the level of customer service. Performance against these measures forms part of the Company's regular reporting to Ofgem.

In respect of the key customer service performance indicators, the Company's performance for the year ended 31 March 2008 showed that it achieved the Ofgem CI target but missed the CML and customer satisfaction targets, as follows:

	Actual	Target
CML:	70.5 (2007: 78.2)	69.5 (2007: 70.4)
CI:	66.3 (2007: 74.0)	74.5 (2007: 74.5)
Customer satisfaction:	88.6% (2007: 88.8%)	90% (2007: 90%)

Operational excellence

The Company's core service continues to be providing and maintaining an efficient distribution network that delivers electricity effectively. During the year, £146.4m was invested in the improvement of the distribution system, including the replacement of assets and continuing network improvements intended to increase the quality of the electricity supply provided to customers.

The investment strategy is designed to deliver improvements in an efficient and cost-effective manner by minimising the number of faults that occur, reducing the average number of customers affected by a fault and providing a quicker restoration service in the event of a fault. Such actions are expected to have a positive impact on future CI and CML performance. The focus in 2008 was on delivering the core operational programmes, in particular the installation of remote control units and improving the lead times for fault repair work-in-progress. The major projects undertaken as part of the investment strategy included:

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DIRECTORS' REPORT (CONTINUED)

Operational excellence (continued)

- The completion of a project to establish a new 66/11kV primary substation at Scarborough;
- The completion of a project to establish a new 66/11kV primary substation at Breamish Street in Newcastle;
- The completion of a 132kV reinforcement project in the Richmond area and the establishment of a single transformer 132kV substation at Skeeby;
- Completion of the overhead line refurbishment works associated with phase two of the refurbishment of the Spennymoor to Skernside 66kV circuit;
- The continuation of a major 33kV reinforcement project in Newcastle designed to meet demand growth and provide further system security in the area;
- Replacement of 60 units of high voltage outdoor switchgear;
- Replacement of 35 high voltage distribution substations;
- Replacement of 40 units of high voltage indoor switchgear;
- Refurbishment or rebuilding of 68km of high voltage overhead line;
- Refurbishment or rebuilding of 22km of low voltage overhead line;
- The upgrade and reinforcement of 2.1km of overhead line to address the quality of supply performance issues relating to those circuits; and
- The installation and commissioning of 300 sites with remote control facilities.

In order to deliver its investment strategy, the Company used a mix of its own staff and contractors to undertake its activities.

In order to help it decide on the priorities for its investment plan, the Company consulted with a wide range of interested parties during the year about its proposals through the publication of a consultation document, which included information about the Company's activities and current priorities and posed a range of questions about its options for the future. The results of that consultation exercise will be considered as part of the discussions regarding the DPCR5 process, which the Company will be conducting with Ofgem throughout 2009.

2008 was the third year in succession to present significant weather-related problems for the distribution network, to which the Company's emergency response process was again effective, particularly in terms of the most severe flooding seen in the Morpeth area for almost 40 years.

Managing commercial risk in the context of the difficult economic and financial trading conditions was and will continue to be of key importance and has seen increased attention being paid by the Company in ensuring that the CE Group's policies for credit checking, payment terms, payment performance tracking and debt management are strictly adhered to.

The Company's main customers are the electricity suppliers who pay Use of System ("UoS") 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.

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DIRECTORS' REPORT (CONTINUED)

Employee commitment

Health and safety

During the year, the focus on health and safety continued to be of paramount importance for the directors, as it is for all employees. Providing and maintaining a safe working environment is the first objective of the Company. There is a continuous drive for improvement in safety performance through the setting of challenging goals and the pursuit of a programme of on-site safety audits, which reflect the Company's fundamental objectives that none of its staff should go home injured and all employees should commit to behaving safely all of the time. 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 received its seventh consecutive Gold Award from the Royal Society for the Prevention of Accidents, for occupational health and safety performance and provision, to recognise the achievement of continued or improving standards of health and safety over a sustained period and continued to maintain its OHSAS 18001 certification.

The main key performance indicators used by the CE Group to monitor safety performance are as follows:

	2008		2007	
	Target	Actual	Target	Actual
Lost time accidents	0	2	0	3
Medical treatment accidents	3	1	1	4
Operational incidents	3	8	4	89
Preventable vehicle accidents	10	18	9	18

Safety performance against target was reasonable in certain areas during 2008 but continued to be somewhat disappointing in others and, following certain events at other platforms in the MidAmerican group, a wide-ranging audit of operational activity was undertaken, aimed at identifying any underlying procedural concerns in respect of operational performance. A number of initiatives arising from that exercise and the continuing evaluation of the lessons to be learned from all safety related incidents have been incorporated into the annual safety improvement plan for 2009, together with an enhanced number of site audits aimed at increasing the focus on operating a safe environment in both the workplace and on the road.

Management structure

The CE Group has a clearly defined leadership team, in which specific roles are identified, so allowing more effective management of the CE Group's business and response to any control weaknesses that may become apparent, with single units being in place for field operations, customer operations, asset management and performance analysis and innovation. The information technology, human resources, procurement and finance functions are centralised in order to provide those services across the CE Group.

Employees

2008 was a particularly challenging year due to the significant industrial relations issues, with which the Company had to deal. Having come through that period with new agreements and understandings in place, the priority for 2009 and beyond will be to constructively engage with the Company's employees through the existing trade union relationships and management structures. The Company will also continue to emphasise the importance of the application of high standards of performance in pursuit of its core principles and will ensure that a level of consistency is adopted in doing so.

The Company employed 959 staff at the end of December 2008 at various locations throughout its distribution services area (2007: 962).

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DIRECTORS' REPORT (CONTINUED)

Employee commitment (continued)

Disabled employees

The Company is an equal opportunities employer and is committed to the criteria underpinning the Employment Service disability symbol. It is the Company's policy to provide disabled people with equal opportunities for employment, training, career development and promotion, having regard to their aptitudes and abilities. Should any member of staff become disabled during their employment, that member of staff would be retrained and redeployed, wherever possible.

Employee consultation

The Company has a constitutional framework in place and has agreed that framework with trade union representatives. In addition, the Company communicates directly, and through the management structure, with personal contract holders and keeps them informed of and involved as appropriate in any developments that may impact on them now or in the future.

The Company is committed to maintaining and improving effective communication with employees, principally through regular staff briefs on current issues, meetings with staff and their representatives and the issue of newsletters and a quarterly employee magazine.

Environmental respect

The CE Group's approach to environmental compliance is governed by its RESPECT policy of Responsibility, Efficiency, Stewardship, Performance, Evaluation, Communication and Training, which includes the promotion of environmental awareness, best practice and legal compliance amongst its staff and contractors.

The CE Group has operated a scheme under the environmental management systems ("EMS") standard ISO 14001 since the late 1990s and is subject to regular six-monthly assessments by an external certification body in order to retain that status. Lloyd's Register for Quality Assurance visited the CE Group in September 2008.

That visit concluded that the four minor non-conformances identified in February 2008 could be closed and raised one new minor non-conformance in respect of depot related operational control issues and noted a minor finding regarding the oil testing programme to verify the polychlorinated byphenyls content of oil in certain categories of transformer assets. The report in respect of the visit concluded that "based on the evidence presented, ... the company is able to demonstrate a sound approach to the implementation, maintenance and improvement of a mature EMS conforming to ISO 14001".

Improvements in support of the CE Group's environmental policy objectives during the year included:

- A programme to enhance secondary containment provision for primary transformer sites to prevent oil leakage;
- A programme to enhance emergency response provision for primary transformer sites to mitigate oil leakage;
- Replacement of oil-filled circuit breakers with vacuum and SF6 units at outdoor substations;
- Improved monitoring and response measures with regard to the management of fluid-filled underground cable networks;
- Installation of additional engineering controls where required to improve pollution prevention in strategic sites;
- Installation of underground cables using trenchless technology as opposed to open-cut excavations;

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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DIRECTORS' REPORT (CONTINUED)

Environmental respect (continued)

- The evaluation of waste management provision and minimisation options together with systematic verification of the legal duty of care in connection with waste management activities;
- Monthly monitoring and management of fuel consumption by fleet vehicles;
- Environmental awareness training for all new start personnel and contractors, complemented by periodic refresher training for all staff; and
- Monthly monitoring of energy consumption at all premises.

Measurements used to monitor environmental performance include the following categories:

- An annual internal environmental management systems audit programme: (29 audits completed) (2007: 38);
- Internal environmental management systems non-conformances: (10 reported and addressed) (2007: 6);
- Continual improvement programmes: (10 underway and performing to target) (2007: 7 underway, with 6 performing to target and 1 temporarily delayed);
- Environmental incidents log: (37 investigated and remedial action taken, including 12 reported to the Environment Agency) (2007: 37 investigated and remedial action taken, including 10 reported to the Environment Agency);
- Cable fluid losses: (an average annual rate of 26.7 litres per kilometre) (2007: 26.2 litres per kilometre);
- Primary transformer oil losses: (zero litres) (2007: 57 litres);
- Secondary transformer oil losses: (1,248 litres) (2007: 2,441 litres);
- All other oil losses: (30 litres) (2007: 69 litres);
- SF6 switch-gear losses: (1.6 kg) (2007: 0.6 kg); and
- Environmental customer communications: (235, mainly substation related, regarding graffiti, weeds and fly-tipping) (2007: 307).

The environmental key performance indicators are made available for scrutiny during the six-monthly external assessments and used by senior management to determine how the system is performing. They measure the delivery of system evaluation and continual improvement programmes, as well as detected non-conformances, reported incidents and the significance of environmental impacts and are subject to on-going monitoring as part of the CE Group's continual improvement programme.

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 CAPSG continued to monitor and manage performance in risk-related and compliance areas and met on four occasions throughout the year.

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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DIRECTORS' REPORT (CONTINUED)

Regulatory integrity (continued)

The benefits associated with upgrading the Company's financial systems continued to be seen in terms of improvements in financial reporting and control and the controls in respect of the UoS process were subject to scrutiny by an internal audit. In addition, the regulatory compliance process was embedded across the Company and includes the provision of quarterly reports to the board. Focus on the accuracy of regulatory returns has continued and positive comments were received from the external consultants who reviewed the systems for PAS 55 accreditation.

The regulatory framework across the energy industry in the UK is undergoing a wholesale review, which could result in fundamental changes to the way the industry is regulated in the future. A significant part of that process is Ofgem's "RPI-X@20" project, which is specifically considering the way in which energy networks are regulated. This review is running alongside the DPCR5 process and the Company has and will continue to take an active part in the debate, which ranges from the potential for new technologies, such as "smart" metering, and the increased use of micro and distributed generation to the low carbon agenda insofar as it applies to electricity distribution networks.

OTHER DIRECTORS' REPORT REQUIREMENTS

Corporate social responsibility

The Company values its relationship with its customers and their communities, recognising the importance of a secure power supply to the local communities and economy and aims to enhance its relationship through a wider involvement in the activities of and dialogue with the communities it serves.

As part of its customer service strategy, the Company engages directly with the communities it serves to create a dialogue on quality of supply issues, actions and investment planned to improve quality of supply, environmental and social implications of its operations and other opportunities to assist and engage in the life of the community. Where appropriate, this may include financial support for community projects. The Company has a targeted donations programme, focusing on its key priorities of support for youth, education and the environment, using both its own funds and income from trusts established with Community Foundations in Tyne and Wear, County Durham and Cleveland.

The CE Group is an active member of Business in the Community.

Charitable and political donations

During the year, charitable donations of £34,649 were made (2008: £65,508), principally to local charities serving the communities in which the Company operates. No contributions were made to political organisations (2007: nil).

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. The main areas of activity during the year were:

- Active participation in programmes of national significance in collaboration with other DNOs and academic institutions to make significant technological progress for utilisation by the industry as a whole;
- Continuing to support collaboration with other DNOs, both through industry associations and on a multilateral basis, on a range of incremental improvements to tools and equipment that, if successful, will further add to overall efficiency improvements;
- Continuing to support the development of a novel (super-conducting) fault current limiter, to reduce prospective short-circuit currents. The resultant lower stress on switchgear, if the project succeeds, will permit the connection of more rotating plant (including generation) with lower levels of reinforcement and/or replacement;

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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DIRECTORS' REPORT (CONTINUED)

Research and development (continued)

- Taking a key role in the set-up and successful start up of the Energy Innovation Centre to provide a portal for technologies and suppliers new to the DNO industry;
- The development of a technology roadmap to provide a fund of potential technical improvement projects that represent state of the art thinking and technology;
- Continuing to support a project at Durham University to assess electrical network risk with the objective of improving decision making on network reinforcement and operation;
- The development of options for automatic voltage control on the LV network; and
- The development of several different fault passage indicator systems to improve reaction time to network faults and minimise customer impact.

Supplier payment policy

The Company complies with the Better Payment Practice Code for the prompt payment of suppliers in accordance with the normal terms of trade. It is CE Group policy with respect to its suppliers to settle the terms of payment with those suppliers when agreeing the terms of each transaction, to ensure that those suppliers are aware of the terms of payment and to pay in accordance with the CE Group's contractual and other legal obligations. The number of days purchases in trade creditors for the Company at 31 December 2008 was 11 (2007: 8).

Future Developments

The financial position of the Company, as at the year end, is shown in the balance sheet on page 22, there have been no significant events since the year end and the directors intend to develop the business in a manner that concentrates on its core skills of electricity distribution by continuing to operate its business with the goal of out-performing the allowances in the distribution price control, while efficiently investing in its electricity distribution system with the aim of improving the quality of supply provided to its customers.

Directors

The directors who served during the year and since the year end were as follows:

G E Abel	President, MidAmerican Energy Holdings Company
P E Connor	Senior Vice President & Chief Procurement Officer, MidAmerican Energy Holdings Company
R Dixon	Non Executive Director
J M France	Regulation Director, CE Electric UK
N M Gill	Field Operations Director
P A Jones	President and Chief Operating Officer, CE Electric UK
K Linge	Finance Director, CE Electric UK

Details of the directors' emoluments are included in note 7 to the accounts.

Auditors

On 1 December 2008, Deloitte & Touche LLP changed its name to Deloitte LLP. An elective resolution is in place dispensing with the need to appoint auditors annually. Deloitte LLP has indicated its willingness to continue in office.

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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DIRECTORS' REPORT (CONTINUED)

Going Concern

The Company's business activities, together with details regarding its future development, performance and position are set out in the Business Review in the Directors' Report. In addition, the Company's objectives, policies and processes for managing its capital, its financial risk management objectives, details of its financial instruments and hedging activities and its exposures to credit risk and liquidity risk are included in the Directors' Report and the appropriate notes to the accounts.

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

- a) In accordance with standard condition 31 of the Company's electricity distribution licence, Berkshire Hathaway, Inc., the ultimate controlling party of the Company, has provided an undertaking that it will procure that any person (including a corporate body), which is a subsidiary of or is controlled by it, will refrain from any action, which would cause the Company to breach any of its obligations under the Electricity Act 1989 or under its electricity distribution licence. The Company's electricity distribution licence includes the obligation in standard condition 40 to maintain an investment grade issuer credit rating;
- b) Explicit support has been made available to MidAmerican by Berkshire Hathaway Inc., which consists of a \$3.5 billion equity commitment that expires on 28 February 2011 and to which the Company has access, if necessary. No amounts were outstanding on that facility as of the date of approval of the Company's accounts to 31 December 2008;
- c) As part of a review of licensees' financing requirements, on 15 January 2009 Ofgem issued an information request to all DNOs under standard licence condition 6 relating to the financial resources each DNO has available in the 24 months ended 31 December 2009. After making enquiries and taking account of several factors, the directors approved the submission to Ofgem of a certificate confirming their reasonable expectation that the Company has, or will have available to it, sufficient financial resources and/or financial facilities to enable the Company to carry on its regulated business for a period of two years since the date of the last statutory accounts;
- d) Under section 3A of the Electricity Act 1989, the Gas and Electricity Markets Authority has a duty, in carrying out its functions, to have regard to the need to secure that licence holders are able to finance the activities, which are the subject of obligations imposed by or under Part 1 of the Electricity Act 1989 or the Utilities Act 2000; and
- e) The Company has considerable financial resources, in the form of short-term borrowings made available by YEG and committed revolving credit facilities from Lloyds TSB Bank plc and Royal Bank of Scotland plc. These credit facilities are due to expire in April 2010, at which point the Company expects to raise further finance as required. The directors do not consider there to be any doubt over the Company's ability to raise such finance, given the investment grade issuer credit ratings held by the Company and due to the fact that the Company operates within a stable and traditionally low risk industry. As a consequence, the directors believe that the Company is well placed to manage its business risks successfully despite the current uncertain economic outlook.

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 annual report and accounts.

Responsibility of directors for the preparation of the report and accounts

The directors are responsible for preparing the Annual Report and the financial statements. The directors are required to prepare financial statements for the Company in accordance with International Financial Reporting Standards ("IFRS") and have also elected to prepare financial statements for the Company in accordance with IFRS. Company law requires the directors to prepare such financial statements in accordance with IFRS, the Companies Act 1985 and Article 4 of the IAS Regulation.

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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DIRECTORS' REPORT (CONTINUED)

Responsibility of directors for the preparation of the report and accounts (continued)

International Accounting Standard 1 requires that financial statements present fairly for each financial year the Company's financial position, financial performance and cash flows. This requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the International Accounting Standards Board's 'Framework for the Preparation and Presentation of Financial Statements'. In virtually all circumstances, a fair presentation will be achieved by compliance with all applicable International Financial Reporting Standards.

Directors are also required to:

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

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company, for safeguarding the assets, for taking reasonable steps for the prevention and detection of fraud and other irregularities and for the preparation of a directors' report which complies with the requirements of the Companies Act 1985. The directors are responsible for the maintenance and integrity of the Company 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 is aware, there is no relevant audit information of which the Company's auditors are unaware; and
- b) he has taken all the steps he ought to have taken as a director in order to make himself aware of any relevant audit information and to establish that the auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of S234ZA of the Companies Act 1985.



By order of the board
John Elliott
Company Secretary

31 March 2009

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF NORTHERN ELECTRIC DISTRIBUTION LIMITED

We have audited the financial statements of Northern Electric Distribution Limited ("the Company") for the year ended 31 December 2008 which comprise the Income Statement, the Statement of Recognised Income and Expense the Balance Sheet and the Cash Flow Statement and the related notes 1 to 26. These financial statements have been prepared under the accounting policies set out therein.

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

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements.

In addition we report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any further information outside the Annual Report.

Basis of audit opinion

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

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

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF NORTHERN ELECTRIC DISTRIBUTION LIMITED (CONTINUED)

Opinion

In our opinion:

- the financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Company's affairs as at 31 December 2008 and of its profit for the year then ended;
- the financial statements have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the financial statements.



Deloitte LLP

Chartered Accountants and Registered Auditors
Newcastle, United Kingdom

 2009

NORTHERN ELECTRIC DISTRIBUTION LIMITED**REGISTERED NUMBER 2906593****INCOME STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2008**

	Notes	2008 £m	2007 £m
Revenue	3	214.9	212.9
Cost of sales		<u>(5.9)</u>	<u>(6.1)</u>
Gross profit		209.0	206.8
Distribution costs		(66.7)	(64.4)
Administrative expenses		<u>(60.4)</u>	<u>(52.5)</u>
Operating profit	5	81.9	89.9
Finance costs	4	<u>(24.1)</u>	<u>(22.6)</u>
Profit before tax		57.8	67.3
Income tax expense	8	<u>(22.7)</u>	<u>(11.1)</u>
Profit for the financial year	21	<u>35.1</u>	<u>56.2</u>

All activities relate to continuing operations.

STATEMENT OF RECOGNISED INCOME AND EXPENSE FOR THE YEAR ENDED 31 DECEMBER 2008

There has been no other income or expense for the Company, other than the profits reported above, in the current or the prior year.

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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BALANCE SHEET AS AT 31 DECEMBER 2008

	Notes	2008 £m	2007 £m
Non-current assets			
Property, plant and equipment	10	1,319.4	1,211.9
Intangibles	11	5.8	6.7
		<u>1,325.2</u>	<u>1,218.6</u>
Current assets			
Inventories	13	8.2	8.3
Trade and other receivables	14	34.9	43.0
Cash and cash equivalents	14	5.2	-
		<u>48.3</u>	<u>51.3</u>
Total assets		<u>1,373.5</u>	<u>1,269.9</u>
Current liabilities			
Trade and other payables	15	(43.7)	(51.6)
Current income tax liabilities	15	(5.6)	(8.2)
Borrowings	16	(96.8)	(43.0)
Deferred revenue	18	(12.5)	(10.3)
Provisions	19	(1.9)	(1.3)
		<u>(160.5)</u>	<u>(114.4)</u>
Net current liabilities		<u>(112.2)</u>	<u>(63.1)</u>
Non-current liabilities			
Borrowings	16	(347.5)	(347.4)
Deferred income tax liabilities	17	(134.2)	(126.3)
Deferred revenue	18	(385.5)	(350.6)
Provisions	19	(0.6)	(1.1)
		<u>(867.8)</u>	<u>(825.4)</u>
Total liabilities		<u>(1,028.3)</u>	<u>(939.8)</u>
Net assets		<u>345.2</u>	<u>330.1</u>
Equity			
Share capital	20	200.0	200.0
Retained earnings	21	145.2	130.1
Total equity	21	<u>345.2</u>	<u>330.1</u>

The financial statements were approved by the board of directors and authorised for issue on 31 March 2009 and were signed on its behalf by:



J M France
Director

NORTHERN ELECTRIC DISTRIBUTION LIMITED

REGISTERED NUMBER 2906593

CASH FLOW STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2008

	Notes	2008 £m	2007 £m
Net cash from operating activities	22	<u>73.3</u>	<u>87.0</u>
Investing activities			
Purchase of property, plant and equipment		(144.2)	(140.6)
Purchase of intangible assets		(0.7)	(2.0)
Proceeds from disposals of property, plant and equipment		0.3	-
Receipt of customer contributions		<u>46.3</u>	<u>41.0</u>
Net cash used in investing activities		<u>(98.3)</u>	<u>(101.6)</u>
Financing activities			
Equity dividends paid		(20.0)	(20.0)
New borrowings		17.0	11.0
Movement in loans from Group undertaking		<u>33.2</u>	<u>23.6</u>
Net cash generated from financing activities		<u>30.2</u>	<u>14.6</u>
Net increase in cash and cash equivalents		5.2	-
Cash and cash equivalents at beginning of year		-	-
Cash and cash equivalents at end of year		<u>5.2</u>	<u>-</u>

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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NOTES TO THE ACCOUNTS - 31 DECEMBER 2008

1 GENERAL INFORMATION

Northern Electric Distribution Limited is a company incorporated in England and Wales under the Companies Act 1985 (the "Act"). The address of the registered office is Lloyds Court, 78 Grey Street, Newcastle-upon-Tyne, NE1 6AF.

The nature of the Company's operations and its principal activities are set out in the Business Review, in the Director's Report and in Note 3.

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 IFRSs adopted by the European Union and therefore comply with Article 4 of the EU IAS Regulation and with those parts of 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 228 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 Company's business activities, together with details regarding its future development, performance and position are set out in the Business Review in the Directors' Report. In addition, the Company's objectives, policies and processes for managing its capital, its financial risk management objectives, details of its financial instruments and hedging activities and its exposures to credit risk and liquidity risk are included in the Directors' Report and the appropriate notes to the accounts.

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

- In accordance with standard condition 31 of the Company's electricity distribution licence, Berkshire Hathaway, Inc., the ultimate controlling party of the Company, has provided an undertaking that it will procure that any person (including a corporate body), which is a subsidiary of or is controlled by it, will refrain from any action, which would cause the Company to breach any of its obligations under the Electricity Act 1989 or under its electricity distribution licence. The Company's electricity distribution licence includes the obligation in standard condition 40 to maintain an investment grade issuer credit rating;
- Explicit support has been made available to MidAmerican by Berkshire Hathaway Inc., which consists of a \$3.5 billion equity commitment that expires on 28 February 2011 and to which the Company has access, if necessary. No amounts were outstanding on that facility as of the date of approval of the Company's accounts to 31 December 2008;
- As part of a review of licensees' financing requirements, on 15 January 2009 Ofgem issued an information request to all DNOs under standard licence condition 6 relating to the financial resources each DNO has available in the 24 months ended 31 December 2009. After making enquiries and taking account of several factors, the directors approved the submission to Ofgem of a certificate confirming their reasonable expectation that the Company has, or will have available to it, sufficient financial resources and/or financial facilities to enable the Company to carry on its regulated business for a period of two years since the date of the last statutory accounts;
- Under section 3A of the Electricity Act 1989, the Gas and Electricity Markets Authority has a duty, in carrying out its functions, to have regard to the need to secure that licence holders are able to finance the activities, which are the subject of obligations imposed by or under Part 1 of the Electricity Act 1989 or the Utilities Act 2000; and

NORTHERN ELECTRIC DISTRIBUTION LIMITED

REGISTERED NUMBER 2906593

NOTES TO THE ACCOUNTS - 31 DECEMBER 2008

2 ACCOUNTING POLICIES (CONTINUED)

Going Concern (continued)

- The Company has considerable financial resources, in the form of short-term borrowings made available by YEG and committed revolving credit facilities from Lloyds TSB Bank plc and Royal Bank of Scotland plc. These credit facilities are due to expire in April 2010, at which point the Company expects to raise further finance as required. The directors do not consider there to be any doubt over the Company's ability to raise such finance, given the investment grade issuer credit ratings held by the Company and due to the fact that the Company operates within a stable and traditionally low risk industry. As a consequence, the directors believe that the Company is well placed to manage its business risks successfully despite the current uncertain economic outlook.

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 annual report and accounts.

Judgements in applying accounting policies and key sources of estimation uncertainty

Many of the amounts included in the financial statements involve the use of judgement and/or estimation. These judgements 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 judgements 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 judgement 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 projects; and
- Impairment reviews carried out to evaluate the carrying value of assets held at the balance sheet 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.

NORTHERN ELECTRIC DISTRIBUTION LIMITED

REGISTERED NUMBER 2906593

NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)

2 ACCOUNTING POLICIES (CONTINUED)

Adoption of new or revised standards

In the current year, the Company has adopted the following interpretation:

IFRIC 12 Service Concession Arrangements

The adoption of IFRIC 12, which is effective for annual periods beginning on or after 1 January 2008, has had no material impact on the financial statements of the Company.

At the date of authorisation of these financial statements there were standards and interpretations in issue but not yet effective, which have not yet been applied in these financial statements. The directors consider that the following may be relevant to the Company in future periods.

IAS 1	Presentation of Financial Statements – “Amendments to IAS 1”
IAS 23	Borrowing Costs – “Amendments to IAS 23”
IFRIC 18	Customer Contributions
IFRS 7	Financial Instruments: Disclosures – “Amendments to IFRS 7”

The directors anticipate that the adoption of the amendments to IAS 1 and IFRIC 18 in future periods will have no material impact on the financial statements of the Company. The amendments to IFRS 7 require enhanced disclosures about fair value measurement and liquidity risk. The amendments to IAS 23, Borrowing Costs, will be adopted from its effective date of 1 January 2009. From this date, borrowing costs will be capitalised in line with the revised standard. The impact of the adoption of IAS 23 in the Company's 2009 financial statements is expected to be approximately £0.6m.

The IASB project “2008 Annual Amendments to IFRSs” was published on 22 May 2008. This project will require presentational changes in the financial statements of the Company for annual periods beginning on or after 1 January 2009.

The directors anticipate the Company will adopt these standards and interpretations on their effective dates.

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, 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.

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)

2 ACCOUNTING POLICIES (CONTINUED)

Revenue (continued)

Customer contributions towards distribution system assets are included in deferred revenue. The Company's policy is to credit the customer contribution to revenue over 45 years 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 income statement in the year in which it is incurred.

Operating profit

Operating profit is stated before investment income and finance costs.

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 income statement 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 balance sheet 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 balance sheet 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 balance sheet 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 balance sheet 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.

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)

2 ACCOUNTING POLICIES (CONTINUED)

Property, plant and equipment and depreciation (continued)

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
Metering equipment included in distribution system assets	up to 15 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.

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 balance sheet and amortised 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.

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)

2 ACCOUNTING POLICIES (CONTINUED)

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 balance sheet 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 balance sheet date.

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 income statement 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 income statement 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 income statement 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.

Financial instruments

Financial assets and financial liabilities are recognised on the balance sheet when the Company becomes a party to the contractual provisions on the instrument.

Financial assets are assessed for indicators of impairment at each balance sheet 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.

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)

2 ACCOUNTING POLICIES (CONTINUED)

Financial instruments (continued)

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 income statement.

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 Electric Group of the Electricity Supply Pension Scheme (the "Northern Electric Group of the ESPS"). The Northern Electric 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 Electric Group of the ESPS as if it were a defined contribution scheme. Contributions to the Northern Electric Group of the ESPS are charged to the income statement or capitalised as appropriate. The capital costs of ex-gratia and supplementary pensions are normally charged to the income statement in the period in which they are granted.

The Company also participates in a defined contribution scheme. Contributions payable to the defined contribution scheme are charged to the income statement in the year. Differences between contributions payable in the year and contributions actually paid are shown as either accruals or prepayments in the balance sheet.

3 REVENUE

Revenue, profit before tax and net assets are attributable to electricity distribution. Revenue is all in respect of sales to United Kingdom customers.

Revenue represents charges made to customers for use of the distribution system, the recharge of costs incurred on behalf of related parties, amortisation of customer contributions and other services and is included net of value added tax.

4 FINANCE COSTS

	2008 £m	2007 £m
Interest payable on loans from Group undertakings	<u>24.1</u>	<u>22.6</u>

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)

5 OPERATING PROFIT

	2008 £m	2007 £m
This is stated after charging/(crediting):		
Staff costs (Note 6)	42.3	35.4
Research costs	0.5	0.4
Depreciation of property, plant and equipment	40.2	38.7
Amortisation of deferred revenue	(10.6)	(9.5)
Amortisation of intangibles	1.7	1.5
Impairment loss/(gain) on trade and other receivables	<u>0.3</u>	<u>(0.3)</u>
Analysis of auditors' remuneration is as follows:	£000	£000
Fees payable to the Company's auditors for the audit of the Company's annual accounts	<u>110</u>	<u>97</u>

There were no fees payable in relation to non-audit services in 2008 or 2007.

6 STAFF COSTS

	2008 £m	2007 £m
Salaries	35.3	33.9
Social security costs	3.1	3.5
Defined benefit pension costs	30.8	23.1
Defined contribution pension costs	<u>0.1</u>	<u>0.1</u>
	69.3	60.6
Less charged to property, plant and equipment	<u>(27.0)</u>	<u>(25.2)</u>
	<u>42.3</u>	<u>35.4</u>

The 2007 split of total costs between salaries and other has been revised with no impact on prior year results.

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

The average monthly number of employees during the year was:

	2008 No.	2007 No.
Technical	250	234
Industrial	449	450
Administration	202	217
Other	<u>64</u>	<u>64</u>
	<u>965</u>	<u>965</u>

NORTHERN ELECTRIC DISTRIBUTION LIMITED**REGISTERED NUMBER 2906593****NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)****7 DIRECTORS' & KEY PERSONNEL REMUNERATION**

DIRECTORS' REMUNERATION	2008 £	2007 £
<u>Highest Paid</u>		
Short-term employee benefits	103,612	98,598
Post employment benefits	9,767	44,560
Other long-term benefits	101,708	108,714
	<u>215,087</u>	<u>251,872</u>
 <u>Total</u>		
Short-term employee benefits	403,641	438,739
Post employment benefits	117,051	130,883
Other long-term benefits	325,208	334,729
	<u>845,900</u>	<u>904,351</u>
 Directors who are members of the defined benefit scheme	<u>6</u>	<u>6</u>
 Accrued pension benefit relating to highest paid director	<u>-</u>	<u>47,270</u>
 OTHER KEY PERSONNEL REMUNERATION	2008 £	2007 £
<u>Total</u>		
Short-term employee benefits	282,281	287,711
Post employment benefits	70,179	57,737
Other long-term benefits	88,588	100,137
	<u>441,048</u>	<u>445,585</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.

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

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)

8 INCOME TAX EXPENSE

	2008		2007	
	£m	£m	£m	£m
Tax expense comprises:				
Current tax expense:				
Corporation tax charge for the year	5.2		13.8	
Payments for use of group losses	9.4		6.8	
Under provision for prior years	0.2		0.4	
Total current tax charge		14.8		21.0
Deferred tax:				
Deferred tax expense relating to the origination and reversal of temporary differences	1.5		(0.8)	
Effect of changes in tax rates	-		(9.1)	
Effect of changes in legislation	6.4		-	
Total deferred tax charge/(credit)		7.9		(9.9)
Tax on profit before tax		22.7		11.1
The total charge can be reconciled to the accounting profit as follows:				
Profit before tax		57.8		67.3
Tax on profit before tax at standard rate of corporation tax in United Kingdom of 28.5% (2007: 30%)		16.5		20.2
Effect of changes in tax rates		-		(9.1)
Effect of changes in legislation		6.4		-
Over provision for prior years		(0.2)		-
Tax on profit before tax		22.7		11.1

The tax rates used are the UK corporate rate of 30% until 31 March 2008 and 28% from 1 April 2008, time apportioned for 2008.

Under IFRS, there is an increase in the year in the deferred tax liability provided on Industrial Buildings. This is due to the change in legislation introduced by the Finance Act 2008.

9 DIVIDENDS

	2008	2007	2008	2007
	Pence per share	Pence per share	£m	£m
Dividend paid	10.0	10.0	20.0	20.0

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)

10 PROPERTY, PLANT AND EQUIPMENT

	Distribution system £m	Fixtures and equipment £m	Total £m
COST			
At 1 January 2007	1,237.5	17.3	1,254.8
Additions	128.2	1.0	129.2
Disposals	(1.8)	(0.4)	(2.2)
At 31 December 2007	1,363.9	17.9	1,381.8
Additions	146.4	1.3	147.7
Disposals	(4.0)	(0.2)	(4.2)
At 31 December 2008	1,506.3	19.0	1,525.3
ACCUMULATED DEPRECIATION			
At 1 January 2007	120.4	13.0	133.4
Charge for the year	36.9	1.8	38.7
Disposals	(1.8)	(0.4)	(2.2)
At 31 December 2007	155.5	14.4	169.9
Charge for the year	38.5	1.7	40.2
Disposals	(4.0)	(0.2)	(4.2)
At 31 December 2008	190.0	15.9	205.9
Net book value at 31 December 2008	1,316.3	3.1	1,319.4
Net book value at 31 December 2007	1,208.4	3.5	1,211.9
Assets in the course of construction included above:			
At 1 January 2007	89.9	-	89.9
Additions	128.2	-	128.2
Available for use	(130.8)	-	(130.8)
At 31 December 2007	87.3	-	87.3
Additions	146.4	-	146.4
Available for use	(154.5)	-	(154.5)
At 31 December 2008	79.2	-	79.2

The Company has entered into contractual commitments in relation to the future acquisition of property, plant and equipment of £6.7m (2007: £23.5m).

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)

11 INTANGIBLES

	Software Development Costs £m
COST	
At 1 January 2007	14.7
Additions	<u>2.0</u>
At 31 December 2007	16.7
Additions	<u>0.8</u>
At 31 December 2008	<u>17.5</u>
AMORTISATION	
At 1 January 2007	8.5
Charge for the year	<u>1.5</u>
At 31 December 2007	10.0
Charge for the year	<u>1.7</u>
At 31 December 2008	<u>11.7</u>
Net book value at 31 December 2008	<u>5.8</u>
Net book value at 31 December 2007	<u>6.7</u>

12 INVESTMENTS

Details of the principal investments of the Company at 31 December 2008 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
Gemserv Limited	England and Wales	1 at £1	0.0004%	Meter point registration
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	2.0%	Management and governance of the Distribution Connection and Use of System Agreement
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 (2007: £62), Gemserv Limited £1 (2007: £1), MRA Service Company Limited £1 (2007: £1), DCUSA Limited £1 (2007: £1) and Northern Electric Finance plc £50,000 (2007: £50,000).

NORTHERN ELECTRIC DISTRIBUTION LIMITED**REGISTERED NUMBER 2906593****NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)****13 INVENTORIES**

	2008 £m	2007 £m
Raw materials and consumables	8.0	7.9
Work in progress	0.2	0.4
	<u>8.2</u>	<u>8.3</u>

14 OTHER FINANCIAL ASSETS**Trade and other receivables**

	2008 £m	2007 £m
Distribution use of system receivables	26.3	33.9
Amounts receivable from sale of goods and services	4.8	5.5
Prepayments and accrued income	3.8	3.5
Treasury instruments	-	0.1
	<u>34.9</u>	<u>43.0</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 balance sheet date. The maximum exposure to risk to the Company is the book value of these receivables less any provisions for impairment.

Distribution use of system receivables

The Company's distribution customers are concentrated in a small number of electricity supply businesses with RWE NPower plc accounting for approximately 36% of distribution revenues in 2008 (2007: 40%). 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 £1.6m as at December 2008 (2007: £1.6m).

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 £0.4m, which have been placed into administration and have therefore been provided in full at the year end.

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 customer contributions in relation to distribution system assets 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 ELECTRIC DISTRIBUTION LIMITED

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NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)

14 OTHER FINANCIAL ASSETS (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 £0.3m (2007: £0.6m) which are past due at the reporting date and for which the Company has provided an irrecoverable amount of £0.1m (2007: £0.4m) based on past experience. The Company does not hold any collateral over these balances. The average age of these receivables is 640 days (2007: 557 days).

Included in the Company's amounts receivable for goods and services balance are debtors with a carrying amount of £1.0m (2007: £0.6m). 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 90 days (2007: 88 days).

Ageing of past due but not impaired receivables

	2008 £m	2007 £m
30-60 days	0.5	0.2
60-120 days	0.2	0.3
120-210 days	0.3	0.1
Total	<u>1.0</u>	<u>0.6</u>

Movement in the allowance for doubtful debts

	£m
At 1 January 2008	0.3
Amounts utilised/written off in the year	(0.1)
Amounts recognised in income statement	<u>0.3</u>
At 31 December 2008	<u>0.5</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 receivable 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 there is no further credit provision required in excess of the allowance for doubtful debts.

Included in the allowance for doubtful debts are specific trade receivables, with a balance of £0.4m (2007: £nil) 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.

Cash and cash equivalents

Cash and cash equivalents comprises cash held at bank. The fair value of cash and cash equivalents is equal to their book value.

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)

15 OTHER FINANCIAL LIABILITIES

Trade and other payables

	2008 £m	2007 £m
Payments received on account	13.6	16.1
Trade payables	3.2	2.9
Amounts owed to Group undertakings	0.4	3.9
Other taxes and social security costs	3.1	2.9
Accruals	21.7	22.4
Other payables	1.7	3.4
	<u>43.7</u>	<u>51.6</u>

Current income tax liabilities

	2008 £m	2007 £m
Corporation Tax	<u>5.6</u>	<u>8.2</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 balance sheet date. 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.

The following tables detail the remaining contractual maturities for the non-derivative financial liabilities included in Notes 15 and 16. The tables have been drawn up based on the discounted 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
2008:					
Non-interest bearing	30.1	-	-	-	30.1
Variable interest rate liability	93.2	-	-	-	93.2
Fixed interest rate liability	-	22.5	89.9	733.1	845.5
	<u>123.3</u>	<u>22.5</u>	<u>89.9</u>	<u>733.1</u>	<u>968.8</u>
2007:					
Non-interest bearing	32.8	6.9	15.7	-	55.4
Variable interest rate liability	43.0	-	-	-	43.0
Fixed interest rate liability	-	22.4	89.6	755.2	867.2
	<u>75.8</u>	<u>29.3</u>	<u>105.3</u>	<u>755.2</u>	<u>965.6</u>

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)

16 BORROWINGS

	Book value		Fair value	
	2008 £m	2007 £m	2008 £m	2007 £m
Loans	28.1	11.0	28.1	11.0
Amounts owed to Group undertakings	416.2	379.4	423.6	405.4
	<u>444.3</u>	<u>390.4</u>	<u>451.7</u>	<u>416.4</u>
The borrowings are repayable as follows:				
On demand or within one year	96.8	43.0	96.8	43.0
After five years	347.5	347.4	354.9	373.4
	<u>444.3</u>	<u>390.4</u>	<u>451.7</u>	<u>416.4</u>
Analysis of borrowings:				
Short term loan	28.1	11.0	28.1	11.0
Inter-company working capital loan	65.2	32.0	65.2	32.0
Northern Electric Finance plc 2020 – 8.875%	101.8	100.0	122.6	127.4
Northern Electric Finance plc 2035 - £50m 5.125%	49.2	47.4	43.5	47.0
Yorkshire Electricity Group plc 2037 – 5.9%	100.0	100.0	94.2	105.1
Northern Electric Finance plc 2037 – 5.125%	100.0	100.0	84.1	93.9
	<u>444.3</u>	<u>390.4</u>	<u>437.7</u>	<u>416.4</u>

The directors' estimates of the fair value of the Company's borrowings are calculated by discounting their future cash flows at the market rate at the balance sheet date.

Interest on the inter company working capital and short term loans is charged at a floating rate of interest at LIBOR plus 0.25%, 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 £0.9m 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.

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.

NORTHERN ELECTRIC DISTRIBUTION LIMITED

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NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)

16 BORROWINGS (CONTINUED)

The Company's Senior Total Net Debt as at 31 December 2008 totalled £438.0m. Using the RAV value as at March 2009, as outlined by Ofgem in its Final Proposals for Distribution Prices published in November 2004, and up rating for the effects of movements in the value of the Retail Price Index gives an approximation for the RAV value as at December 2008 of £827.1m. The Senior Total Net Debt to RAV ratio for the Company is therefore estimated at 53%.

At 31 December 2008, the Company had available £24.0m (2007: £41.0m) of undrawn committed borrowing facilities in respect of which all conditions precedent had been met.

17 DEFERRED TAX

	Accelerated Tax Depreciation £m	Other £m	Total £m
At 1 January 2007	136.8	(0.6)	136.2
(Credit)/charge to income statement	(10.1)	0.2	(9.9)
At 31 December 2007	126.7	(0.4)	126.3
Charge to income statement	7.9	-	7.9
At 31 December 2008	134.6	(0.4)	134.2

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

18 DEFERRED REVENUE

	£m	
At 1 January 2007	336.7	
Additions	33.7	
Amortisation	(9.5)	
At 31 December 2007	360.9	
Additions	47.7	
Amortisation	(10.6)	
At 31 December 2008	398.0	
	2008 £m	2007 £m
Included in current liabilities	12.5	10.3
Included in non-current liabilities	385.5	350.6
	398.0	360.9

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

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NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)

19 PROVISIONS

	Claims £m	Other £m	Total £m
At 1 January 2008	1.4	1.0	2.4
Utilised/paid in the year	(1.0)	(0.1)	(1.1)
Charged to the income statement	0.9	0.3	1.2
At 31 December 2008	<u>1.3</u>	<u>1.2</u>	<u>2.5</u>
		2008 £m	2007 £m
Included in current liabilities		1.9	1.3
Included in non-current liabilities		<u>0.6</u>	<u>1.1</u>
		<u>2.5</u>	<u>2.4</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.

20 SHARE CAPITAL

	2008 No./£	2007 No./£
Ordinary shares of £1 each		
Authorised	300,000,000	300,000,000
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.

21 MOVEMENT ON RESERVES AND RECONCILIATION OF MOVEMENTS IN TOTAL EQUITY

	Share Capital £m	Retained Reserves £m	Total Equity £m
At 1 January 2007	200.0	93.9	293.9
Profit for the year	-	56.2	56.2
Dividends paid	-	(20.0)	(20.0)
At 31 December 2007	200.0	130.1	330.1
Profit for the year	-	35.1	35.1
Dividends paid	-	(20.0)	(20.0)
At 31 December 2008	<u>200.0</u>	<u>145.2</u>	<u>345.2</u>

NORTHERN ELECTRIC DISTRIBUTION LIMITED**REGISTERED NUMBER 2906593****NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)****22 NET CASH FROM OPERATING ACTIVITIES**

	2008 £m	2007 £m
Operating profit	81.9	89.9
Depreciation and amortisation	41.9	40.2
Amortisation of deferred revenue	(10.6)	(9.5)
Increase in provisions	0.1	0.2
	<hr/>	<hr/>
Operating cash flows before movements in working capital	113.3	120.8
Decrease/(increase) in inventories	0.1	(1.3)
Decrease/(increase) in receivables	7.0	(3.4)
(Decrease)/increase in payables	(2.1)	15.7
	<hr/>	<hr/>
Cash generated by operations	118.3	131.8
Income taxes paid	(8.1)	(10.5)
Group relief paid	(9.3)	(10.5)
Dividends received	0.1	-
Interest paid	(27.7)	(23.8)
	<hr/>	<hr/>
Net cash from operating activities	73.3	87.0

23 PENSION COMMITMENTS

The Company has two retirement benefit schemes.

The Northern Electric Group of the ESPS is a defined benefit scheme for directors and employees, which provides pension and other related benefits based on final pensionable pay. The assets of the Northern Electric Group of the ESPS, which was closed to staff commencing employment on or after 23 July 1997, are held in a separate trustee-administered fund. The Northern Electric Money Purchase Scheme was made available to new employees from that date.

The Northern Electric Group of the ESPS and the Northern Electric Money Purchase Scheme are operated by Northern Electric plc on behalf of the participating companies within the CE Group.

The last full actuarial valuation of the Northern Electric Group of the ESPS was carried out by the Group Trustees' actuarial advisors, Hewitt Associates, as at 31 March 2007. The projected unit method was used for the valuation. The principal actuarial assumptions were that pre retirement investment returns would exceed salary increases by 1.8% per annum (inclusive of merit awards) and post retirement returns would exceed future pension increases by 1.8% per annum.

The total market value of the assets of the Northern Electric Group of the ESPS, at the date of the actuarial valuation, was £926.7m.

For the Northern Electric Group of the ESPS, the actuarial valuation showed that the value of the assets represented 90.7% of the actuarial value of the accrued benefits. This represents a shortfall of assets compared to the value of accrued benefits of £95.1m. The accrued benefits include all benefits for pensioners and other former members, as well as benefits based on service completed to date for active members, and allows for an estimate of future salary increases.

NORTHERN ELECTRIC DISTRIBUTION LIMITED

REGISTERED NUMBER 2906593

NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)

23 PENSION COMMITMENTS (CONTINUED)

The CE Group reached agreement during March 2008 with the Group Trustees to repair this deficit. The agreement comprises monthly cash payments of £2.4m (£28.8m per annum) backdated to commence in April 2007 in addition to the normal employer contributions. Of these annual payments, £21.9m will be paid by the Company. These payments aim to remove the shortfall of £95.1m by December 2010 subject to the actuarial assumptions adopted for the triennial valuation as at 31 March 2007 being borne out in practice.

The Northern Electric Group of the ESPS 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 net defined benefit cost for the plan as a whole to individual group entities and accordingly the Company accounts for the scheme as if it were a defined contribution scheme.

The contribution rates to the Northern Electric Group of the ESPS, in addition to the deficit repair contributions mentioned above, for 2008 were 44.7% (60.7% to March 2008) for certain senior management and 26.3% (20.6% to March 2008) for other employees. These rates will remain in place until 31 March 2010.

The money purchase pension scheme is also accounted for as a defined contribution scheme.

The Company pension cost for the year ended 31 December 2008 was £30.9m (2007: £23.2m).

Disclosures in relation to the Northern Electric Group of the ESPS are:

Principal assumptions:

	2008	2007
Valuation method	Projected unit	Projected unit
Discount rate	6.40%	5.90%
Inflation rate	3.00%	3.20%
Increase to pensions	3.00%	3.20%
Increase to deferred benefits	3.00%	3.20%
Salary increases	3.25%	3.45%

The mortality assumptions are based on the recent actual mortality experience of members within the CE Group and the assumptions also allow for future mortality improvements. The assumption is that a member currently aged 60 will live for a further 26 years, if he is male, and for a further 27 years, if she is female. Life expectancy at age 60 for non-pensioners (currently aged 45) is assumed to be 28 years, if they are male, and 28 years, if they are female.

For closed schemes, such as the Northern Electric Group of the ESPS, under the projected unit method the current service cost will increase as the members of the scheme approach retirement.

NORTHERN ELECTRIC DISTRIBUTION LIMITED

REGISTERED NUMBER 2906593

NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)

23 PENSION COMMITMENTS (CONTINUED)

Changes in present value of the defined benefit obligation are as follows:

	2008 £m	2007 £m
Opening defined benefit obligation	917.2	925.9
Current service cost	10.3	11.9
Interest cost	53.0	47.2
Contributions from employees	3.1	3.5
Actuarial gains	(87.3)	(32.0)
Benefits paid	(41.0)	(39.3)
Closing defined benefit obligation	<u>855.3</u>	<u>917.2</u>

Changes in the fair value of the plan assets are as follows:

	2008 £m	2007 £m
Opening fair value of plan assets	956.6	912.8
Expected returns	66.2	63.9
Actuarial losses	(231.4)	(19.6)
Contributions by employer	47.9	35.3
Contribution from employees	3.1	3.5
Benefits paid	(41.0)	(39.3)
Closing fair value of plan assets	<u>801.4</u>	<u>956.6</u>

The fair value of the plan assets at the balance sheet date is analysed below:

	Long term rates of return expected at		Value	
	2008 %	2007 %	2008 £m	2007 £m
Equities	8.90	8.90	322.2	388.7
Gilts	5.35	5.10	404.7	445.3
Cash	3.25	6.00	(4.8)	23.3
Property	7.90	7.90	79.3	99.3
Total fair value of scheme assets			<u>801.4</u>	<u>956.6</u>

The CE Group employs a building block approach in determining the long-term rate of return on pension plan assets. Historical markets are studied and assets with higher volatility are assumed to generate higher returns consistent with widely accepted capital market principles. The assumed long term rates of return on each asset class are set out within these disclosures. The overall expected rate of return on assets is then derived by aggregating the expected return for each asset class over the actual asset allocation for the Northern Electric Group of the ESPS.

The CE Group expects to contribute approximately £44.1m to its defined benefit plan in 2009, including £28.4m of pension deficit repair costs.

NORTHERN ELECTRIC DISTRIBUTION LIMITED**REGISTERED NUMBER 2906593****NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)****24 OPERATING LEASE ARRANGEMENTS**

	2008 £m	2007 £m
Minimum lease payments under operating leases recognised in the year	<u>6.7</u>	<u>6.0</u>

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

	2008 £m	2007 £m
Within one year	4.1	4.3
In the second to fifth year inclusive	13.3	13.4
After five years	<u>18.7</u>	<u>20.9</u>
	<u>36.1</u>	<u>38.6</u>

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

25 RELATED PARTY TRANSACTIONS

The Company has received loans from other companies in the CE Group. The total interest included in finance costs in the income statement for the year ended 31 December 2008 was £24.1m (2007: £22.6m). Included within borrowings is £416.2m as at 31 December 2008 (2007: £379.4m) and within trade and other payables £nil as at 31 December 2008 (2007: £3.6m) in respect of these loans.

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

NORTHERN ELECTRIC DISTRIBUTION LIMITED**REGISTERED NUMBER 2906593****NOTES TO THE ACCOUNTS - 31 DECEMBER 2008 (CONTINUED)****25 RELATED PARTY TRANSACTIONS (CONTINUED)**

The Company entered into transactions, in the ordinary course of business, with other CE Group companies. Transactions entered into and trading balances outstanding were as follows:

Related Party	Sales to Related Party £m	Purchases from Related Party £m	Amounts Owed to Related Party (Note 15) £m
2008:			
CE Insurance Services Limited	-	0.7	-
Integrated Utility Services Limited(registered in Eire)	-	1.0	0.2
Northern Electric plc	0.3	4.8	-
Northern Electric Properties Limited	-	1.0	-
Yorkshire Electricity Distribution plc	9.8	6.1	-
Vehicle Lease and Service Limited	-	2.7	0.2
2007:			
CE Insurance Services Limited	-	0.6	-
Integrated Utility Services Limited (registered in Eire)	0.1	1.1	-
Northern Electric plc	0.2	6.2	-
Northern Electric Properties Limited	-	0.9	-
Yorkshire Electricity Distribution plc	9.3	5.8	-
Vehicle Lease and Service Limited	-	3.0	0.3

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

26 IMMEDIATE PARENT UNDERTAKING AND CONTROLLING PARTY

The immediate parent undertaking of Northern Electric Distribution 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 Electric Distribution Limited and the group accounts of Northern Electric plc, the smallest parent undertaking to prepare group accounts in the UK, can both be obtained from the Company Secretary, CE Electric UK Funding Company, Lloyds Court, 78 Grey Street, Newcastle upon Tyne, NE1 6AF.