

**STRATEGIC REPORT, REPORT OF THE DIRECTORS AND
CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2013
FOR
NORTHERN POWERGRID HOLDINGS COMPANY**

REGISTERED NUMBER: 03476201

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FOR THE YEAR ENDED 31 DECEMBER 2013**

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NORTHERN POWERGRID HOLDINGS COMPANY

**COMPANY INFORMATION
FOR THE YEAR ENDED 31 DECEMBER 2013**

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**STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2013**

The directors present the annual reports and accounts of Northern Powergrid Holdings Company (the "Company") and its subsidiary companies (together the "Group") for the year ended 31 December 2013, which includes the Strategic Report, the Report of the Directors and the audited financial statements for that year. Pages 2 to 19 inclusive of this annual report comprise the Strategic Report and pages 19 to 29 comprise the Report of the Directors, which have been drawn up and presented in accordance with the Companies Act 2006.

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 the Group 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.

**STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2013**

BUSINESS MODEL

The Company is the ultimate parent undertaking for the Group in the United Kingdom and its main subsidiary companies are Northern Powergrid (Northeast) Limited ("Northeast") and Northern Powergrid (Yorkshire) plc ("Yorkshire") (together the "Distribution Business"), Integrated Utility Services Limited, registered in the United Kingdom, ("IUS"), CalEnergy Resources Limited ("CE Gas") and Integrated Utility Services Limited, registered in the Republic of Ireland ("IUS Ireland").

Northeast and Yorkshire are distribution network operators ("DNOs") and distribute electricity to a total of approximately 3.9 million customers connected to their electricity distribution networks at voltages of up to 132kV, IUS and IUS Ireland provide engineering contracting services and CE Gas holds interests in hydrocarbon permits in Australia, Poland and the United Kingdom.

The Group operates a business model and strategy based on its six core principles (the "Core Principles"), which are:

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

STRATEGIC OBJECTIVES

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

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

**STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2013**

STRATEGIC OBJECTIVES - continued

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

REVIEW OF THE YEAR

The Group delivered a satisfactory financial performance for the year, which benefited from a further reduction in the rate of taxation and continued effective cost control. However, that performance fell slightly short of plan due to a rebate totalling £28.5 million, which the Distribution Business made to the electricity suppliers as part of the Government-led initiative to assist domestic customers with their energy bills and will be recovered by the Distribution Business in future years.

Ofgem finalised its price control policies early in 2013 in respect of the next regulatory period, which will run from 1 April 2015 to 31 March 2023 and is known as ED1. One of the main priorities for the Distribution Business in 2013, therefore, was the preparation of its well-justified business plan, which was submitted for Ofgem's consideration on 28 June 2013. Ofgem announced on 22 November 2013 that it had decided that the Distribution Business' plan was not to proceed on the "fast track" and, while recognising that the Distribution Business had submitted a strong plan, had certain reservations about the future cost efficiency and asset replacement elements. Although that decision was disappointing, most if not all of the commitments made in the Distribution Business' plan will stand and, in order to deliver on those commitments, work has already begun to change the way the Distribution Business operates. Following Ofgem's decision, the Distribution Business revisited its plan and provided Ofgem with a revised version including further justification of the associated costs on 17 March 2014.

Having delivered its largest ever capital expenditure programme to date in 2012, the Distribution Business continued with its policy to invest efficiently in its electricity distribution networks. During the year, the Distribution Business invested £443.9 million in its distribution networks such that it improved on its performance in 2012 and remains well-placed in respect of the outputs it intends to deliver by the end of the current Distribution Price Control period to 31 March 2015 ("DPCR5").

The Distribution Business continued to design and deliver initiatives to improve the quality of service provided to its customers and, while recognising that improvements still have to be made in order to meet its targets, maintained the upward trend in its customer service performance. As delivery of the capital expenditure programme, the provision of excellent customer service and ensuring a reliable electricity supply are some of the most significant outputs the Distribution Business is required to deliver during DPCR5, the directors are confident that the performance delivered in 2013 maintains the strong basis for a successful conclusion to DPCR5 developed over the preceding three years.

The Distribution Business introduced an online application process in April 2013, which allows customers to apply for a new connection quickly, easily and conveniently. Work also began on developing an online self-quotation service for high volume connections customers which, when launched, will deliver a significant reduction in the overall time to serve those customers. When taken with other services such as 'ask our expert', an indicative pricing tool and a small scale embedded generation single connection notification process, the Distribution Business was the first DNO to offer customers such a wide variety of connection services online. The Distribution Business again beat Ofgem's targets for the quality of the electricity supply provided to its customers and continued to focus on reducing the average times taken to restore supplies following a power cut.

Environmental performance continued to be strong with the Distribution Business' response time to environmentally-related network events improving such that fewer incidents were reportable to the Environment Agency than in 2012. Less oil was lost to the ground during the year than in 2012 despite the on-going issue of interference with the Distribution Business' assets by third parties intent on metal theft. Given the impact on the environment of such events, the Distribution Business included a commitment to reducing losses from fluid-filled cables in its well-justified business plan by replacing a significant number of those assets on a phased and prioritised basis over ED1 and increasing the use of perfluorocarbon tracers to improve the efficiency of oil leak identification.

**STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2013**

REVIEW OF THE YEAR - continued

The long-term trend in the Group's overall safety performance continued to compare well with that of the industry but the internal targets were missed in respect of lost time accidents. Preventable vehicle accident performance missed target but improved on that delivered in 2012 and represented the Group's best ever performance. Seven lost time accidents occurred in 2013, which was three more than in the previous year, with one of those lost time accidents being an electrical contact incident, which had the potential to be more serious than the ultimate outcome. In addition, an employee of a contractor to Northeast tragically died while working on the network. That incident was subject to an investigation by the Health and Safety Executive, which concluded with the Health and Safety Executive not taking any further action against Northeast.

Activity levels in the UK Contracting area of IUS' business in the North of England increased in comparison to 2012 and IUS successfully secured contracts in its Rail activities that significantly increased revenue in 2013. IUS also saw an increase in the number of orders across all areas of its business with the improved forward order book in place at the end of 2013 for delivery in 2014 creating a solid foundation for achieving anticipated future growth.

CE Gas continued to develop its portfolio of hydrocarbon exploration, construction and producing assets in Australia, Poland and the United Kingdom. During the year, an appraisal well was drilled in the Whicher Range in Australia to further evaluate recoverable hydrocarbons. There will be further evaluation work on the Whicher Range discovery in 2014 including critical well flow testing. CE Gas also progressed the Concept Select process for both the Baltic Gas Project (offshore to Poland) and the Platypus discovery (offshore to the United Kingdom). During the final quarter of 2013 NewGen Drilling Pty Limited commenced operations of its Australian based land rig.

CORE PRINCIPLES

Financial strength

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

The Distribution Business benefits from the stability provided by the arrangements agreed in respect of DPCR5 in terms of its income until 31 March 2015 and recognises that it needs to show that it is delivering reliable services at a fair price to its customers, while operating in an efficient and effective manner.

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

Revenue

The Group's revenue at £722.0 million was £25.9 million higher than the prior year mainly due to additional allowances arising from the settlement in respect of DPCR5 and increased contracting revenues, partly offset by the rebate paid to electricity suppliers noted on page 4.

Operating profit and position at the year end

The Group's operating profit at £366.4 million was £3.8 million lower than the previous year, with higher costs such as grid connection charges, depreciation and amortisation being partially offset by the increased distribution revenues and contracting gross margin. The consolidated statement of financial position on pages 34 and 35 shows that, as at 31 December 2013, the Group had total equity of £1,563.8 million. The directors consider the Group to have a strong statement of financial position which, when coupled with the preference of its parent company, MidAmerican Energy Holdings Company ("MidAmerican"), for leaving equity in the business, creates a stable base for continued strong performance into ED1 by the Distribution Business.

Finance costs and investments

Finance costs net of investment income at £86.6 million were £1.0 million lower than 2012 reflecting changes in the profile of borrowings during the year and increased capitalised interest.

Taxation

The effective tax rate in the current year is 7% (2012: 7%). The effective tax rate before adjusting for the impact of the changes in tax rates introduced by the Finance Act 2013 and amounts allocated to other comprehensive income would be 24%. Details are provided in Note 7 to the accounts.

**STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2013**

Financial strength - continued

Results and dividends

The Group made a profit after tax for the year of £260.9 million (2012: £263.2 million). No dividend was paid during the year (2012: £Nil) and the directors recommend that no final dividend be paid in respect of the year. Other comprehensive income for the year, net of income tax, was a loss of £16.5 million (2012: loss of £50.0 million).

Share capital and debt structure

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

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

Movements in cash flows were as follows:

Operating activities: Cash flow from operating activities at £293.6 million was £47.1 million higher than the previous year. Favourable working capital movements were offset by lower profits.

Investing activities: Net cash used in investing activities at £404.4 million was £112.6 million higher than the previous year, reflecting higher net capital expenditure.

Financing activities: The net cash generated from financing activities at £61.8 million represents a £6.0 million adverse variance compared to the previous year, reflecting net movements in borrowings in the year.

Liquidity risk

The Distribution Business has access to £150 million under a five year committed revolving credit facility provided by Lloyds Bank plc, The Royal Bank of Scotland plc and Abbey National Treasury Services plc, which expires on 20 August 2017. The Distribution Business expects to raise further facilities, as required, at that time.

In addition, companies in the Group have access to further short-term borrowing facilities provided by YEG. The Distribution Business has an overdraft facility provided by Lloyds Bank plc totalling £42 million, which is reviewed annually.

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

Interest rate risk

The Group 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 2013, 100% of the Group's long-term borrowings were at fixed rates and the average maturity for these borrowings was 13 years.

Currency risk

No material currency risks are faced by the Group.

Pensions

Northern Electric plc ("NE"), a company in the Group, is the principal employer of the Northern Powergrid Group of the Electricity Supply Pension Scheme (the "Scheme"), a defined benefit scheme. Full details of the Group's commitments to the Scheme and the associated deficit repair payments are provided in Note 27 to the accounts.

Companies in the Group also participate in the Northern Powergrid Pension Scheme, which is a defined contribution scheme.

**STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2013**

Financial strength - continued

Insurance

As part of its insurance and risk strategy, the Group has in place a range of insurance policies, including policies which cover risks associated with damage to property, employer's and third party motor liability and public liability. The 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 Distribution Business distributed electricity to customers in its distribution services area and continued to improve the overall performance of the distribution network through an investment strategy targeted at delivering improvements in an efficient and cost-effective manner. The Distribution Business remains focused on delivering a reliable and dependable supply of electricity and a high standard of service to its customers.

The Distribution Business aims to enhance its relationship with various stakeholders through direct engagement on the actions and investment planned to improve the performance of the network and on the environmental and social implications of its operations. Consequently, as part of the process of drafting its well-justified business plan for submission to Ofgem for consideration in respect of ED1, the Distribution Business consulted with a wide range of stakeholders regarding its services. That consultation included formal presentations to large groups, web-based communications and some high quality input from three expert panels, which looked at social issues, low carbon networks and customer service.

Taking account of the views of its stakeholders that were received as part of the consultation process, the Distribution Business took forward its programme to modernise and redesign the customer-facing elements of its business in support of the goal of improving customer satisfaction with the service provided. The various initiatives in that programme included:

- The transformation of the connections business so that it is led by and tailored to meet the requirements of customers in different market segments;
- Extending the means by which the Distribution Business undertakes its stakeholder engagement, which will involve building on the experience gained from the process of drafting the well-justified business plan and by increasing joint initiatives with other utility companies;
- Encouraging uptake of the Distribution Business' online community to facilitate discussion among stakeholders regarding the Distribution Business' services and use of the dedicated web area where stakeholders can provide feedback to influence its policies and priorities and be in continuing contact;
- Further developing customer relationship management information technology, social media and website services to provide more accurate information to customers, particularly in respect of estimated times for the restoration of supply during power cuts and to engage more effectively with and receive feedback from customers;
- Developing and implementing self-service quotation facilities for customers seeking low voltage connections in order to extend the Distribution Business' online transactional capabilities;
- Improving the reliability of under-performing parts of the distribution network by continuing to identify "hot spots" of particularly poor network performance and taking specific action to address the issues in those areas;
- Refreshing and promoting the priority services register so enabling the Distribution Business to be aware of vulnerable customers who may be affected by power cuts so that it can take appropriate action to assist those people in such circumstances, engaging the support of the Red Cross where appropriate;
- Operating customer service vehicles wherever they can assist with the welfare of the Distribution Business' customers and provide support during power cuts; and
- Continuing a programme to provide employees from across the Group with enhanced customer service awareness training and the tools and skills needed to handle power cut calls during periods of peak call demand.

**STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2013**

Customer service - continued

The performance of the DNOs against guaranteed standards, which are set for activities such as restoring supplies after power cuts, provides a measure of the level of customer service. Performance against these measures forms part of the Distribution Business' regular reporting to Ofgem.

Ofgem's incentive scheme for quality of service, by which the DNOs are provided with financial incentives, is based upon targets set by Ofgem with regard to each DNO's performance in terms of the number of power cuts, the duration of those power cuts and customer satisfaction.

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

In respect of these key customer service performance indicators, the goal is to achieve performance that is below Ofgem's target number in respect of CML and CI. The Distribution Business' performance for the year to 31 March 2013 (the "Regulatory Year") was as follows:

	Northeast Actual	Northeast Target	Yorkshire Actual	Yorkshire Target
CML:	70.2 (2012: 68.5)	70.9 (2012: 71.1)	62.8 (2012: 65.0)	76.0 (2012: 76.0)
CI:	64.9 (2012: 67.9)	68.2 (2012: 68.2)	72.2 (2012: 69.3)	75.3 (2012: 75.3)

Performance in the Regulatory Year was better than Ofgem's target for both CML and CI and contributed to the Distribution Business' improved customer service performance in the year.

The Regulatory Year was the third year in which the Ofgem discretionary reward for stakeholder engagement had been in operation and the first year that a financial incentive had been available. Building on the good performance in its stakeholder engagement over the Regulatory Year, the Distribution Business put forward a submission for consideration by Ofgem's panel, which achieved a score of 78.5%. As a result, the Distribution Business was ranked as the third placed DNO group and secured a reward which could total up to £0.9 million for the Group.

Under the Broad Measure of Customer Service, an independent market research company, Accent, carries out telephone surveys with the Distribution Business' customers to find out how satisfied they are with the services provided. During the Regulatory Year, Accent surveyed a number of customers who had contacted the Distribution Business regarding an unplanned or a planned power cut, had requested a price quotation and a subsequent connection or had a general enquiry where a service had been provided or a job completed. Northeast recorded an overall satisfaction score of 77.9% and Yorkshire of 78.1% for the Regulatory Year and the Distribution Business expects that its customer service improvement plan, including the range of initiatives noted on page 7, will improve the services provided to customers and so increase the satisfaction rating year-on-year.

Connections to the network

During the year, the Distribution Business continued to improve the connections services provided to its customers, while also actively facilitating the development of competition from independent connections providers ("ICPs"), so providing increased choice to customers in the region. The Distribution Business continued to engage regularly with its connections customers in groups and individually, holding monthly customer surgeries, twice yearly customer events and contributing to national stakeholder forums and events.

Taking account of feedback from such events, the Distribution Business introduced an online application process in April 2013, which allows customers to apply for a new connection quickly, easily and conveniently. Work also began on developing an online self-quotation service for high volume connections customers which, when launched, will deliver a significant reduction in the overall time to serve those customers. Other online services include 'ask our expert', an indicative pricing tool and a small scale embedded generation single connection notification process. The Distribution Business was the first DNO to offer customers such a wide variety of connection services online.

**STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2013**

Customer service - continued

Connections to the network - continued

As part of the DPCR5 final proposals, Ofgem put in place a competition test to encourage all of the DNOs to make it easier for ICPs to provide competing offers to customers and, in line with Ofgem's deadline for submission, the Distribution Business put forward a case to prove that competition exists in eight market segments. This is in addition to the high voltage segment, in respect of which the Distribution Business passed Ofgem's test in October 2012. It is expected that Ofgem will make a determination in respect of the Distribution Business' submission by the end of April 2014.

Although there was a substantial reduction in volumes of housing and new development works due to the recession, connection requests for low carbon generation have remained very buoyant with the area covered by the Distribution Business being one of the busiest for such developments in the UK. Interest in the development of solar farms has begun to increase more recently and, as the new housing market starts to recover, the Distribution Business is seeing an increase in the number of requests for connections of new housing to the network.

The Distribution Business continues to seek feedback from its customers on a regular basis in order to assist with developing further improvements to its services and, in that respect, its connections customers have been instrumental in shaping the Distribution Business' strategy regarding the structure required of its connections business in preparation for ED1. The services provided in future will be tailored to the requirements of customers in the different market segments so that the Distribution Business provides a faster and more flexible service.

Corporate responsibility

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

The Distribution Business maintained its key partnerships with the Environment Agency, the local authorities and the local resilience forums, via a Civil Contingency Co-ordinator, so that it can respond quickly to significant faults on or threats to the network. In the event that river levels rise and flood warnings are issued, staff can be deployed immediately to erect perimeter flood defences at major substation sites and portable defence barriers at lower risk sites. In addition, the Distribution Business has well-established emergency procedures that are triggered in times of weather-related incidents or long-duration power cuts when people are without power for some time. The Distribution Business responded well to a number of major weather-related incidents during the year, which impacted on its assets, including the highest tidal surges along the East coast for a number of years in early December.

As well as redeploying staff from planned works to help restore power as quickly as possible when major incidents occur, the Distribution Business has a number of customer service vehicles, which are dispatched to the areas affected. Those vehicles are able to distribute hot drinks and to microwave meals and generally assist with the welfare of customers in order to alleviate the impact of the incident. The Distribution Business also utilised its 'customer ambassadors' to address customers' concerns and resolve their complaints and worked with the Red Cross in order to pay particular attention to the welfare of customers on the priority services register so that those customers are kept informed of the situation throughout the event and after the power has been restored. Having begun work to improve the quality of the information held on the priority services register, the Distribution Business is promoting the benefits of being on that register more widely and has revised the criteria for registration so that customers with short-term health or welfare issues are now able to benefit.

The Group has in place a small donation programme, which is focused on its key priorities of support for youth, education and the environment and from which grants were made during the year to organisations such as charitable trusts and community groups.

Safety remains the Group's first priority and underpins every aspect of its operations. During the year, the Distribution Business continued to participate, alongside other key organisations, in 'Crucial Crew', which is a schools-based safety initiative that teaches children to recognise and avoid situations that put them in danger, such as climbing electricity pylons and fishing near power lines. The Distribution Business' school safety programme included Crucial Crew events, school visits, participation in safety days and the "prison me - no way" campaign and is delivered by two dedicated safety presenters who promote the safety messages through an interactive presentation. The programme is also supported through an interactive website and mobile phone game.

**STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2013**

Operational excellence

The Group's core service continues to be providing and maintaining efficient distribution networks that deliver electricity effectively. During the year, £443.9 million was invested in the improvement of the distribution networks, a 5.8% increase on the £419.6 million recorded in 2012. The Distribution Business' continued and substantial investment in its distribution networks has seen reliability increase throughout DPCR5. During that period, an electricity supply has been available to the Distribution Business' customers for approximately 99.98% of the time and the Distribution Business has generally outperformed the targets set by Ofgem in respect of CI and CML. The Distribution Business' inspection and maintenance regimes have ensured that the underlying health of the network assets has been sustained and none of the leading indicators used by the Distribution Business suggest any diminishing performance in this respect in the future.

Operational activity

The Distribution Business continues to implement an investment strategy, which is designed to deliver improvements in an efficient and cost-effective manner in order to improve the networks' resilience. In its well-justified business plan, the Distribution Business committed to enhancing the reliability of the networks such that fewer power cuts affect customers and, when power cuts do happen, they are shorter in duration.

The Distribution Business' Field Operations structure is currently based on six individual business units. Those business units are Network Operations, which provides the day-to-day and reactive management of the network, Service Delivery, which has responsibility for the control and management of the direct labour force, Network Repairs, which focuses on core repair activities, Connections Delivery, which undertakes customer-driven work, Programme Delivery, which includes primary engineering projects and technical services, and Operational Services, which includes supply chain management and training services. As a new guaranteed standard for the restoration of supply within 12 hours of a power cut occurring will apply from 1 April 2015, the Distribution Business began a review of its operational structure in order to provide a more localised focus and, therefore, improved response times in the event of a power cut. If the Distribution Business fails to meet that 12 hour standard, it will make an automatic payment to customers, whenever it is aware of such a failure, rather than customers having to make a claim.

The Distribution Business' priorities during the year included delivering a significant level of capital expenditure on the network, which was higher than that delivered in 2012, a further reduction in the average level of fault repair work in progress, a robust approach to the control of operations on the low voltage network and continued focus on the restoration times associated with both high and low voltage power cuts with high voltage restoration performance averaging some 64 minutes during the year, after allowing for the impact of severe weather incidents.

The major projects undertaken by Northeast in support of those targets and as part of the investment strategy included:

- Completion of works to replace a 66kV transformer at Linton, the 66kV circuit breakers at Cramlington and Grangetown, the 11kV switchgear at Hartmoor substation and the 33kV transformers at Mount Road substation in Sunderland. In addition, major refurbishment works were completed on the transformers at Darlington West and Tynemouth Central substations;
- Continuation of works to reinforce the 33kV network in the Harrogate area, to replace the 66kV circuit breakers at Coalburns substation in Gateshead, to replace the 66kV transformer at Maddison Street, to replace the 66/11kV transformers and 20kV switchgear at Sunderland substation and to replace the 11kV switchgear at Northallerton and Catterick Camp substations;
- Commencement of works to replace the 132kV transformers, the 66kV transformers, the 20kV and the 11kV switchgear at Potterhouse substation in Durham in order to reinforce the network in the Durham area;
- Commencement of major works to install new 33kV transformers and a new 33kV cable circuit to Foss Island substation to reinforce the network in the York area;
- Commencement of works to replace the 132kV transformers in substations at Harraton and Barrack Road in Newcastle city centre and to replace the 66kV assets in substations at Bowesfield, North Tees, Fossway in York and Spencerbeck in Middlesbrough;

**STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2013**

Operational excellence - continued

Operational activity – continued

- Completion of a number of projects across Northeast's distribution services area that replaced 12km of 33kV fluid-filled cables and 3km of 132kV fluid filled cable;
- The completion of refurbishment or rebuilding works on 22km of 33kV and 66kV overhead line, 120km of 132kV overhead line and the refurbishment or rebuilding of 401km of high voltage overhead line and 120km of low voltage overhead line;
- Replacement of 52 units of high voltage outdoor switchgear, 56 high voltage distribution substations and 247 units of high voltage indoor switchgear;
- The upgrade and reinforcement of 28 sites to address the quality of supply performance issues relating to those circuits; and
- The installation and commissioning of 447 new remote control points on the network.

The major projects undertaken by Yorkshire included:

- Completion of the replacement of a 132kV transformer at Halifax substation, the replacement of the 66kV switchgear at Beighton and Wath substations in Sheffield area, the replacement of the 33kV switchgear at Osgodby substation in Selby and the construction of a new 33kV substation to reinforce the network in the Scunthorpe area;
- Completion of major refurbishment works on the 132kV transformers at Girdlington substation in Bradford, Whinmoor substation in Leeds and on the 66kV transformers at Woolley substation near Barnsley;
- Continuation of the replacement of the 132kV circuit breakers at Wold Newton, the 33kV and 11kV assets (including transformers) at Blackburn Valley and the 33kV transformers at Burton Road and Kirk Drive substations;
- Commencement of the replacement of the 132kV transformer at West Melton substation near Rotherham, the 66kV and 11kV assets at South Kirkby substation near Wakefield and a major scheme to reinforce the network in the Doncaster area;
- Completion of a number of projects across Yorkshire's distribution services area that replaced 19km of 33kV fluid-filled cables, 14km of 33kV gas filled cables and 6.5km of 33kV solid cables and the completion of a project that replaced 0.5km of 132kV fluid filled cable;
- Completion of refurbishment works on 46km of 33kV and 66kV overhead line, the refurbishment of 92km of 132kV overhead line and the refurbishment or rebuilding of 244km of high voltage overhead line and 86km of low voltage overhead line;
- Replacement of 73 units of high voltage outdoor switchgear, 90 high voltage distribution substations and 365 units of high voltage indoor switchgear;
- The upgrade and reinforcement of 24 sites to address the quality of supply performance issues relating to those circuits; and
- The installation and commissioning of 373 new remote control points on the network.

In order to deliver its investment strategy, the Distribution Business used a mix of its own staff and contractors to undertake its activities, including affiliated companies in the Group.

**STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2013**

Employee commitment

Health and safety

The focus on health and safety continued to be of paramount importance for the directors, as it is for all employees. There is a continuous drive for improvement in safety performance through the setting of challenging goals and the pursuit of a comprehensive safety and health improvement plan, which reflects the Group's fundamental objective that none of its staff should go home injured and all employees should commit to behaving safely all of the time. The Group 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 Group's safety record over a number of years suggests that it is one of the safest in the electricity distribution and engineering contracting sectors and it will strive to maintain that position over the coming years. Having identified issues that may pose an increased safety risk such as metal theft and the impending roll-out of smart meters, the Distribution Business intends to implement various measures through its safety and health improvement plan that will build incrementally on the existing strong safety record and ensure that safety considerations are always a part of the investment decision-making and appraisal process.

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

	2013		2012	
	Target	Actual	Target	Actual
Lost time accidents	2	7	3	4
Restricted duty accidents	4	2	4	2
Medical treatment accidents	3	1	5	4
Operational incidents	8	15	8	13
Preventable vehicle accidents	26	31	26	35

In common with the MidAmerican group, the Group measures its safety performance in terms of the Occupational Safety and Health Administration ("OSHA") rate, which is a measure used in the United States to capture safety incidents down to minor levels of medical treatment, such as a stitch or the use of prescription pain killers. As part of its plan to reduce the OSHA and preventable vehicle accident rates across the group, MidAmerican issues daily e-mail updates in respect of performance against its overall OSHA rate and preventable vehicle accident targets, which include information on incidents that have occurred.

The Group's safety and health improvement plan targets continuous improvement and delivery of the various initiatives contained in that plan contributed to the Group achieving an OSHA rate of 0.43 against a target of 0.4, which represented its best ever performance.

The Group experienced more lost time accidents than in 2012. One of those lost time accidents was an electrical contact incident, which had the potential to be more serious than the ultimate outcome, and an employee of a contractor to Northeast tragically died while working on the network. The Group worked with the Health and Safety Executive as part of its investigation into that incident, which concluded with the Health and Safety Executive not taking any further action against Northeast. As at 31 December 2013, IUS had worked 1.6 million man hours without incurring a lost time accident.

Performance in respect of preventable vehicle accidents missed the target for 2013 but was better than in 2012 and represented the Group's best ever performance. None of those incidents gave rise to any significant safety-related risks.

As part of the safety and health improvement plan and in order to reinforce the operational safety values, the Group continued to implement its cross-business operational assurance audit programme and introduced a field engagement programme designed to link up the leadership of the Group with its employees in the field for the purposes of improving two-way communication on safety and other key business issues. The Group continued to implement a robust road risk management plan, which involved electronic driving licence checking, delivering road risk awareness workshops to new employees and using risk reduction tools such as online driver assessment and training followed by an on-road refresher training session if required. The driver training programme provides practical driving training to a targeted population of drivers and is the primary route to improving driver skills in the longer term.

**STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2013**

Employee commitment - continued

Health and safety - continued

Following a detailed research and design project, the Group issued innovative protective work wear to its employees during the first quarter of the year, which provides protection against the effects of events such as electrical flashovers. The Group invested a substantial amount in this new clothing, believes that it is unique in the industry and that it will be a significant factor in reducing the risk to its employees. The Group also delivered operational seminars and stand down briefings and issued regular safety newsflashes to staff in order to cascade information on safety trends, issues and incidents.

During the year, Northeast received a President's Award from the Royal Society for the Prevention of Accidents for achieving 12 consecutive Gold Awards and Yorkshire received a President's award for achieving nine consecutive Gold Awards. IUS received its fifth consecutive Gold Medal, which also entitled it to receive a President's Award. Those awards were presented in recognition of achievements in 2012 and for continued or improving standards of health and safety over a sustained period. The Distribution Business continued to maintain its occupational health and safety management system and retained its Occupational Health and Safety Assessment Series ("OHSAS") 18001 certification and environmental management system ISO 14001 certification.

The sickness absence rate for the Group for 2013 was 2.22% (2012: 2.55%), which was an improvement on 2012 and does not give rise to any particular cause for concern.

Management structure

Operational management of the Distribution Business is undertaken by a single senior management team, with specific functional responsibilities. Those functional responsibilities are in respect of field operations, health, safety and environment, asset management (including procurement), commercial (including customer operations and information technology), regulation and strategy, human resources, organisation development and finance. Certain of those functions also provide services across the Group. IUS and CE Gas have their own, separate management teams.

Employees

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

Given the demographics of the Distribution Business' workforce, the increasing investment in the distribution network and in order to encourage investment in a sustainable workforce, Ofgem provided an allowance in its DPCR5 final proposals in order to fund the plans for workforce renewal throughout DPCR5. Ofgem has stated that the allowance is on a "use it or lose it" basis and the Distribution Business will need to demonstrate that it has used that allowance appropriately and efficiently to recruit and train new staff or for other means of renewing its workforce and report annually on its progress in that respect.

The Group recruited a total of 227 members of staff in 2013, including 92 trainees under its workforce renewal programme. A total of 52 trainees recruited under that programme in previous years graduated from their training programmes during 2013 and commenced work as part of the Distribution Business' operations. The plan remains in place to have recruited a total of 275 graduate trainees, technical trainees and craft apprentices by the end of DPCR5.

The Group is committed to proper business conduct and, in common with 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. A "speaking up" policy is in place so that members of staff are able to raise any instances of unethical acts, malpractice or impropriety. An additional process is also available to all staff via an international, anonymous help line operated by an independent company.

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 Group employed 2,541 staff at the end of December 2013 at various locations in the United Kingdom, the Republic of Ireland, Poland and Australia (2012: 2,405).

**STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2013**

Environmental respect

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

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

The most recent visit was a six-monthly surveillance assessment carried out by Lloyd's Register Quality Assurance in September 2013. The assessment report drew management attention to only one minor non-conformance to be addressed by agreed proposed actions. The report also noted that significant improvements had been made to the environmental management system over the past three years. Procedures and processes have been reviewed and developed to improve the effectiveness of the aspects register, legal register and internal audits. Operational controls at depots were also seen to have significantly improved over the past three years which correlated to a reducing number of minor non-conformances raised at surveillance visits. There were no major non-conformances noted and continued certification was recommended and subsequently confirmed.

Improvements in support of the Group's environmental policy objectives included replacing selected fluid-filled cable sections with non-fluid polymeric equivalents, replacing oil-filled circuit breakers with vacuum and sulphur hexafluoride gas filled units at outdoor substations to reduce the potential for oil leakage and using gas tracer technology to locate cable fluid leaks quicker, where it was practicable to do so. In addition, the Distribution Business provided environmental awareness training for new personnel and contractors and periodic refresher training for all staff.

The Group's commitment to the Environmental RESPECT policy and its overall performance shows that it can be relied on to keep its impact on the environment to a minimum. In preparing its well-justified business plan, the Distribution Business engaged directly with the Environment Agency in respect of a number of issues and will continue to maintain strong and open relationships with its various environmental stakeholders, particularly in respect of the network's visual impact. The main environmental elements of the well-justified business plan included significant programmes to replace fluid-filled cables and place overhead lines underground in national parks, reduce electrical losses and implement further improvements to the network that take account of protected structures, features, areas, wildlife and habitat. This includes protecting bird life by placing bird-diverters on power lines where they are in proximity to reserves, wetlands, flight paths or in locations where rare species of bird are known to live or breed and also in response to information obtained from incident trends.

Sustainability

The Group's activities have an important part to play in the United Kingdom's transition to a low carbon economy, both in its capacity as a major participant in the United Kingdom energy industry and in terms of its own carbon footprint. As the country takes action to make significant reductions in its carbon emissions, the way electricity is produced and used is expected to have a significant impact on the electricity networks over time. The Distribution Business is taking actions to be able to demonstrate that its networks will be ready to handle the energy flows its customers need when required and by working with customers to assist in solving issues raised by the installation of low-carbon generation and technologies. The Distribution Business is also actively involved in working with the industry and other interested parties in order to develop national policies and strategies to assist the low-carbon transition.

The Group measures and publishes details of its own carbon footprint and, between 2009 and 2013, reduced its carbon footprint by 13%. The Group has set a target to reduce its carbon footprint by a further 10% over the next 10 years and, in line with Ofgem's requirements, the Distribution Business has contributed to the sustainability agenda through public reporting on its carbon footprint. During the year, the Distribution Business gained re-certification under CEMARS (the Certified Emissions Measurement and Reduction Scheme) that its measurement of its greenhouse gas emissions was in compliance with ISO 14064.

**STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2013**

Environmental respect - continued

Sustainability - continued

The number of installations by customers of low-carbon technologies such as photovoltaic solar panels and heat pumps continued to increase during the year. The greater diversity of demands being placed on the networks arising from the decarbonisation of the energy market means that the Distribution Business needs to develop smart solutions that avoid the need for expensive reinforcement of the network. In that respect, the Group's Customer-Led Network Revolution project aims to learn how novel network technology and changes in customers' energy usage habits may lead to the speedier and lower cost connection of low-carbon technologies to the networks. By the end of 2013, more than 10,000 customers were participating in the trials and installation of the related equipment had been largely completed, with over 500 customers having taken part in a feedback survey and 230 interviews having taken place. Six electrical storage devices have been commissioned, as planned, and the initial results from the monitoring of customers' load profiles, including the impact of time-of-use tariffs, and from industrial and commercial trials of demand side management have been published and presented at over 50 events attended by various interested parties.

The well-justified business plan presented the Distribution Business' proposition for sustainable networks over ED1 including the need for investment in enabling technology, reinforcement of the networks to alleviate the constraints associated with low carbon technologies and supporting the roll-out of smart meters. The Distribution Business believes that its plan will not only create some immediate benefits for customers during ED1 but also pave the way for much greater benefits after 2023.

Regulatory integrity

The Group manages its business to the highest behavioural standards and adheres to a policy of strict compliance with all relevant standards, legislation and regulatory conditions. The Governance and Risk Management Group ("GRMG") monitored and managed performance in risk-related and compliance areas and met on four occasions during the year.

As has been the case for some years, breaches by a DNO of its licence conditions could lead to financial penalties, which Ofgem has stated "will have a proportionate impact on shareholder returns". In order to assure compliance with its licence and other regulatory obligations, the Distribution Business operates a regulatory compliance affirmation process, under which ownership of the approximately 1,700 regulatory obligations contained within the compliance database is currently assigned to around 60 responsible managers. Those responsible managers are required, on a quarterly basis, to review compliance with the relevant obligations that have been assigned to them for certification and report on any identified non-compliances or perceived risks to the compliance process, which are then addressed. The Regulation Manager reports to the boards of Northeast and Yorkshire on the outcome of each quarter's exercise.

A revenue-related issue arose during 2010 in that the adjustment of settlements data by certain suppliers had the effect of distorting the apparent performance of the Distribution Business under the losses incentive scheme for the regulatory year ended 31 March 2010. Throughout 2013, the Distribution Business continued to engage with Ofgem and other industry participants to resolve the complex issues surrounding the losses incentive arrangements for both the current and previous price control periods. Ofgem has removed the DPCR5 losses incentive and, on 21 March 2014, published its decision on the restatement of the 2009/2010 data and closing out the Distribution Price Control Review 4 losses incentive, together with details of the final sums to be returned by Northeast and Yorkshire during ED1. In accordance with International Financial Reporting Standards, the Company has not included any recognition of this issue in these Accounts.

Under the new RIIO (revenue = incentives + innovation + outputs) model for regulation, price controls will be set for eight years (rather than five as at present), with provision for a mid-period review of the outputs that network companies are required to deliver. Ofgem triggered the ED1 review process in the first quarter of 2012 and finalised its price control policies early in 2013, following which the Distribution Business submitted its well-justified business plan for Ofgem's consideration on 28 June 2013. Ofgem announced on 22 November 2013 that it had decided that the Distribution Business' plan was not to proceed on the "fast track" and, while recognising that the Distribution Business had submitted a strong plan, had certain reservations about the future cost efficiency and asset replacement elements. Following Ofgem's decision, the Distribution Business revisited its plan and provided Ofgem with a revised version including further justification of the associated costs on 17 March 2014. Ofgem will now consider the revised plan and discuss the details further with the Distribution Business during the remainder of 2014. A final decision is expected by December 2014 and, on conclusion of the process, the Distribution Business' revenues will be set for the period from 2015 to 2023.

**STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2013**

Regulatory integrity - continued

During the year, the Distribution Business continued its voluntary involvement with the other DNOs in developing and trialling more formalised arrangements for assuring the accuracy of the information returns submitted to Ofgem. This exercise has involved the development of risk-assessment matrices and the preparation and submission to Ofgem of a risk-based data-assurance plan, followed by the submission of a report detailing the assurance work actually carried out and the findings of that work. The DNOs have been joined in the trial by transmission and gas distribution licensees and the new regime will continue to be developed in the light of experience during the year. The finalised arrangements will be incorporated into the licences of all the DNOs in April 2015.

PRINCIPAL RISKS AND UNCERTAINTIES

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

Financial risk

As holders of an electricity distribution licence, Northeast and Yorkshire are subject to regulation by the Gas and Electricity Markets Authority ("GEMA"), which acts through Ofgem. Most of the revenue of the electricity distribution licence holders is controlled by the distribution price control formula set out in the electricity distribution licence. The price control formula does not constrain profits from year to year but sets a maximum permitted revenue for each regulatory year and is a control on revenue that operates independently of most of the electricity distribution licence holder's costs. Where the Distribution Business recovers more, or less, than this maximum the difference is carried forward, with interest, into the entitlement for the following year.

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. A resetting of the formula can now be made by GEMA without the consent of the electricity distribution licence holder but a licensee can appeal to the Competition and Markets Authority against a decision by GEMA to proceed with such a modification. Certain other interested parties have the same right. The current five-year price control period became effective on 1 April 2010 and has set the Distribution Business' revenues through to 31 March 2015.

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

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

However, given the stable and regulated nature of the DNOs' businesses, Ofgem took the view that a notional repair period of 15 years was appropriate for the purpose of assessing the DNOs' allowed revenues in respect of pension costs over DPCR5.

The other financial risks facing the Group are on page 6 of this Strategic Report.

Operational risk

There are a number of risks to the Group's operational performance in respect of which mitigating actions have been taken. Appropriate credit cover arrangements are in place with the electricity suppliers, which would allow recovery of defaulted payments through the price control mechanism and a robust major incident management plan is implemented whenever severe weather impacts on the distribution network's performance. Metal theft continued to be a significant issue for the Distribution Business during the year with the activities of metal thieves causing power cuts on various occasions, which affected a large number of customers in aggregate. In response, the Distribution Business maintained the programme of risk-assessed and enhanced security measures at its sites and pursued awareness raising activity at a national and local level. Those risk mitigation actions were supported by a change in the law which prohibited scrap metal dealers from paying for scrap metal in cash.

**STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2013**

PRINCIPAL RISKS AND UNCERTAINTIES - continued

Operational risk - continued

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

Commercial risk

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

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

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

The Group operates a structured and disciplined approach to the management of risk as part of its overall risk management policy and, in DPCR5 and previous price control periods, has accepted and successfully managed substantial cost and delivery risks by developing a culture of cost and risk management over that period of time. Risks are 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. Those risks assessed to be significantly high are logged within a risk register that the GRMG reviews regularly and key indicators are used to track and monitor those risks considered to be significant.

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 are being implemented. These plans are monitored through to implementation and reviewed to determine whether the residual, mitigated risk is within an acceptable level of tolerance.

The 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 regular review of the key risks, controls and action plans is undertaken. The risk management programme includes regular review of the crisis management, disaster recovery and major incident plans, which are periodically tested, the sharing of best practice on disaster preparedness and response, penetration tests against firewall systems and disaster recovery tests of IT servers and priority processes and a peer review of the Group's risk management systems by MidAmerican.

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

A key element and requirement of the risk management process is that a written certificate is provided by the President and Chief Executive Officer of the 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.

**STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2013**

PRINCIPAL RISKS AND UNCERTAINTIES – continued

Internal Control

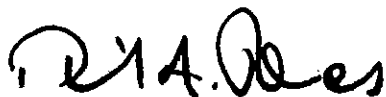
A rigorous internal control environment exists within the Group based on regular reporting, a series of operational and financial policy statements, investigations undertaken by internal audit and a stringent process for ensuring the implementation of any recommendations. MidAmerican requires a quarterly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

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

The Group is committed to preventing corruption in all its forms and continues to have a zero-tolerance approach to corruption in its business or by those with whom it does business. The board has addressed the risks introduced by the Bribery Act 2010 through a compliance policy, changes to contractual terms, training and other staff awareness measures. The introduction of annual risk assessments and enhanced due diligence in respect of new business transactions has further assisted in ensuring compliance. The Group requires staff, suppliers of services and business partners to comply with the Bribery Act. Its policies encourage an employee who has any suspicion of bribery or other form of corruption within or related to the Group to report the suspicion to a manager or via the international, anonymous help line mentioned in the employee section.

The Distribution Business has appropriate controls in place directed at ensuring compliance with the conditions in its licences 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.

ON BEHALF OF THE BOARD:



P A Jones
Director

16 April 2014

**REPORT OF THE DIRECTORS
FOR THE YEAR ENDED 31 DECEMBER 2013**

DIVIDENDS

No dividend was paid during the year (2012: £Nil). The directors recommend that no final dividend be paid in respect of the year.

RESEARCH AND DEVELOPMENT

During the year, Northeast continued working, on behalf of the Group and in partnership with British Gas, Durham University and EA Technology, on its major project under Ofgem's Low Carbon Networks Fund, known as the Customer-Led Network Revolution. This remains the largest project supported by Ofgem in the four years of the fund and Northeast will incur expenditure of £31.0 million over the life of the project. Of that expenditure, 90% is funded by electricity customers in Great Britain. Successful delivery of the project over the period agreed with Ofgem will enable recovery of the additional 10% from customers and potentially qualify for a further discretionary award.

The project is assessing the potential for new network technology and flexible customer response to facilitate speedier and more economical take-up by customers of low-carbon technologies and the connection to the distribution network of increasing amounts of low-carbon or renewable energy generation. 2013 saw further, and increasingly mature, trialling of equipment and operational techniques to allow the efficient application of low carbon technologies on the network. The scale of the project's output is such that additional time has been sought from Ofgem, extending the project to four years, to ensure that the quality of learning delivered is relevant, timely and provides value-for-money for all stakeholders.

The Group also supports a programme of research that is expected to contribute to higher standards of performance and a more cost-effective operation of its business. New activities in voltage stabilisation, real time rating of assets to increase current carrying capacity and improved ultrasonic integrity assessment of overhead line assets have been commissioned. Other work completed during 2013, included the further application of network risk methodologies to a range of business processes, allowing better planning and operational execution, and research to better understand the environmental variation within network substations and its impact on the condition and service lifetime of the Distribution Business' assets.

During the year, the Group invested £12.9 million (2012: £13.8 million) (Note 6 to the accounts) in its research and development activities.

FUTURE DEVELOPMENTS

The financial position of the Group, as at 31 December 2013, is shown in the Consolidated Statement of Financial Position on pages 34 and 35. There have been no significant events since the year end.

During the year, the Group published its well-justified business plan for the future of the Distribution Business and submitted that plan to Ofgem for consideration as part of the ED1 price control review process. That plan set out the Distribution Business' priorities for and the challenges it expects to see during ED1, which will last for the eight years until March 2023. The Distribution Business plans to provide its customers with more for less by improving performance in respect of all of the outputs expected of it, reducing prices in the first year of ED1 and then maintaining those prices at a relatively consistent level over the remainder of the period, delivering 20% shorter power cuts and providing a connections service that is 30% faster, together with a range of new and improved services. Having resubmitted the well-justified business plan for Ofgem's consideration on 17 March 2014, the directors intend to continue to develop the Distribution Business by operating that business with the goal of out-performing the allowances in the price control, while efficiently investing in the network and improving the quality of supply and service provided to its customers.

IUS will continue to develop its business in a manner that concentrates on its core skills of engineering contracting by delivering a high standard of service to its existing clients and pursuing opportunities to increase its portfolio of clients across all regions of the United Kingdom in the sectors within which it operates.

CE Gas will continue to look to build value through the management of a portfolio of hydrocarbon projects in Australia, Poland and the United Kingdom.

**REPORT OF THE DIRECTORS
FOR THE YEAR ENDED 31 DECEMBER 2013**

DIRECTORS

The directors shown below have held office during the whole of the period from 1 January 2013 to the date of this report.

G E Abel	Chairman
D L Anderson	Executive Vice President, General Counsel and Corporate Secretary, MidAmerican Energy Holdings Company
R Dixon	Non-executive Director
J M France	Regulation Director
P J Goodman	Executive Vice-President and Chief Financial Officer, MidAmerican Energy Holdings Company
P A Jones	President and Chief Executive Officer
J N Reynolds	Non-executive Director

FINANCIAL RISK MANAGEMENT

Liquidity risk

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

Trading risk

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

Financial derivatives

As at 31 December 2013 and during the year it was the Group's policy not to hold any derivative financial instruments.

POLITICAL DONATIONS

During the year, no contributions were made to political organisations (2012: £nil).

EMPLOYEES

Employee consultation

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

The Group 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 increased use of the Group's intranet to improve communication and engagement with the workforce.

During the year, the President and Chief Executive Officer delivered quarterly broadcast briefings using telephone conference call facilities in order to provide employees with updates on the Group's financial, organisational, safety and customer service performance and posted weekly blogs on the Group's intranet in order to provide updates on key elements of performance during the preceding week.

Disabled employees

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

**REPORT OF THE DIRECTORS
FOR THE YEAR ENDED 31 DECEMBER 2013**

CORPORATE GOVERNANCE STATEMENT

In September 2012, the Financial Reporting Council published a revised version of the UK Corporate Governance Code (the "Code"). The Company provides the following statement by reference to the main principles in the Code and sets out how it has applied those principles. To the extent that it departs from the Code, the Company explains below from which parts of the Code it departs and the reasons for doing so.

Compliance statement

Set out below and in the review of the year in the Strategic Report are the areas in which the Company adopts and complies with the main principles of the Code. The Company has not complied with certain of the main principles of the Code, including main principles A2, A3, B2, B6, B7, C3, D1, D2 and E2. The directors confirm that such non-compliance was of a continuing nature throughout the year but consider the governance framework in place to be appropriate to the circumstances of the Company, given that the framework is agreed with MidAmerican and includes regular reporting to and meetings with the Chairman and senior management of MidAmerican, the presence of independent non-executive directors at board meetings of the Company and a strong internal control environment designed to meet the standards required by the United States Sarbanes-Oxley Act.

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

Section A: Leadership

Main Principle A1: The Role of the Board

The directors have agreed a schedule of board meetings at which they review general business performance, strategy and operational and risk-related issues. In addition, the President and Chief Executive Officer participates in weekly performance review meetings with the Chairman of MidAmerican and other senior managers of the MidAmerican group, including the Executive Vice President and Chief Financial Officer. At those weekly meetings, the views of the Chairman of MidAmerican and the senior management team regarding the key, current issues facing the Group are discussed.

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

The board meets as required to consider relevant issues and met on five occasions in total during the year, with the attendance of the directors being as follows:

G E Abel	Chairman	0
D L Anderson	Executive Vice President, General Counsel and Corporate Secretary, MidAmerican	0
R Dixon	Non-Executive Director	5
J M France	Regulation Director	4
P J Goodman	Executive Vice-President and Chief Financial Officer, MidAmerican Energy Holdings Company	0
P A Jones	President and Chief Executive Officer	4
J N Reynolds	Non-Executive Director	4

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

**REPORT OF THE DIRECTORS
FOR THE YEAR ENDED 31 DECEMBER 2013**

CORPORATE GOVERNANCE STATEMENT - continued

Section A: Leadership - continued

Main Principle A1: The Role of the Board - continued

The directors have overall responsibility for the internal control environment, which, within the Group, is based on regular reporting, a series of operational and financial policy statements, investigations undertaken by internal audit and a stringent process for ensuring the implementation of any recommendations. In addition, MidAmerican 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 United States Sarbanes-Oxley Act. The assessments undertaken during the year did not identify any significant weaknesses in the process but resulted in the implementation of various recommended improvements. The key features of the Group's internal control system and the issues addressed by the Group during the year can be found in the Strategic Report.

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

During the year, there were a number of committees in operation, acting under delegated terms of reference, which oversee Group policy. As part of the approved terms of reference, certain of those committees report regularly to the board on their activities and are as follows:

Health and Safety Management Committee

The board has established the Northern Powergrid Group Health and Safety Management Committee with delegated powers to manage the health and safety policy and performance of the Group. Membership of the committee comprises:

J P Barnett	Commercial Director
G M Earl	Director of Safety, Health and Environment
T E Fielden	Finance Director
J M France	Regulation Director
N M Gill	Field Operations Director
P A Jones	President and Chief Executive Officer
A J MacLennan	Managing Director, Integrated Utility Services Limited and Integrated Utility Services Limited (registered in Eire)

The committee meets on a regular basis in order to oversee implementation of the health and safety policy, review and agree strategy for the management of health and safety issues, monitor health and safety performance across the Group, review the effectiveness of the health and safety policies and the health and safety management system and consider recommendations for changes in policy due to changes in appropriate legislation, codes of practice or guidance or due to recommendations arising from significant incidents.

Treasury Committee

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

G E Abel	Chairman, MidAmerican
D Brady	Treasurer
T E Fielden	Finance Director
P J Goodman	Executive Vice President and Chief Financial Officer, MidAmerican
S Gormally	Corporate Accountant and Secretary to the Committee
P A Jones	President and Chief Executive Officer
S J Lockwood	Group Financial Controller
O Sutherland	Investor Reporting Manager

**REPORT OF THE DIRECTORS
FOR THE YEAR ENDED 31 DECEMBER 2013**

CORPORATE GOVERNANCE STATEMENT - continued

Section A: Leadership - continued

Main Principle A1: The Role of the Board - continued

Pensions Committee

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

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

Governance and Risk Management Group

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

D Anderson	Head of Internal Audit
J P Barnett	Commercial Director
R Dixon	Non-Executive Director
M Drye	Director of Asset Management
G Earl	Director of Safety, Health and Environment
J Elliott	Company Secretary
T E Fielden	Finance Director
J M France	Regulation Director
N M Gill	Field Operations Director
L Hutchinson	Director of Human Resources
A J MacLennan	Managing Director, Integrated Utility Services Limited and Integrated Utility Services Limited (registered in Eire)
O Sutherland	Investor Reporting Manager

The risk management framework was monitored regularly during the year to ensure that all strategic risks, including those relating to environmental and social issues, were being addressed. Risk management policies and procedures were reviewed and updated to ensure a robust and clear approach was maintained. Mr Dixon attended meetings of the GRMG to provide an independent view in respect of the matters discussed.

Asset risk continued to be a strong focus through the Asset Risk Management Executive Review Group and comprehensive plans continued to be in place to manage risks affecting all critical property assets and to strengthen the arrangements for crisis management and business continuity planning.

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

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

**REPORT OF THE DIRECTORS
FOR THE YEAR ENDED 31 DECEMBER 2013**

CORPORATE GOVERNANCE STATEMENT - continued

Section A: Leadership - continued

Main Principle A2: Division of Responsibilities

Mr G E Abel, the Chairman of MidAmerican, is Chairman of the Company. As President and Chief Executive Officer, Dr Jones is responsible for the operation and management of both the Group and the Group and reports directly to Mr Abel.

Main Principle A3: The Chairman

Dr Jones chairs board meetings and is responsible for the operation and management of the Group and reports directly to Mr Abel.

Main Principle A4: Non-Executive Directors

There are two independent non-executive directors on the board of the Company, Mr Dixon and Mr Reynolds, who act under agreed terms of reference

Section B: Effectiveness

Main Principle B1: The composition of the board

The board comprises five executive directors and two independent non-executive directors, who, collectively, bring a range of skills and experience to the board. Although the board does not include a balanced number of executive and non-executive directors, the board believes that it possesses the skills and experience necessary to provide effective leadership, stewardship and control of the Company and the Group.

Main Principle B2: Appointments to the board

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

Main Principle B3: Commitment

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

Main Principle B4: Development

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

Main Principle B5: Information and support

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

**REPORT OF THE DIRECTORS
FOR THE YEAR ENDED 31 DECEMBER 2013**

CORPORATE GOVERNANCE STATEMENT - continued

Section B: Effectiveness - continued

Main Principle B6: Evaluation

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

Main Principle B7: Re-election

The directors retire by rotation and offer themselves for re-election in accordance with the Company's articles of association.

Section C: Accountability

Main Principle C1: Financial and business reporting

The board believes that the Strategic Report and the Report of the Directors provide a balanced and understandable assessment of the Group's position and prospects. The directors explain, at page 3 of the Strategic Report, the Core Principles behind the Group's strategy and, at page 27 in the Report of the Directors, their responsibility for preparing the Strategic Report, the Report of the Directors and the accounts, have reported, at page 27 in the Report of the Directors, that the Company and the Group are going concerns and have included the Report of the Independent Auditor to the Company at pages 30 and 31 of these accounts.

Main Principle C2: Risk management and internal control

Details of the principal risks and uncertainties facing the Group and its internal control system, together with details of the issues addressed by the Group during the year, can be found at pages 17 to 19 of the Strategic Report.

Other key features of the internal control system are:

- Comprehensive business planning and financial reporting procedures, including the annual preparation of detailed operational budgets for the year ahead and projections for subsequent years;
- Regular review of key performance indicators to assess progress towards objectives;
- A range of policies, codes of practice and more detailed instructions that define the processes to be followed;
- A strong internal audit function, which provides independent scrutiny of internal control systems and risk management procedures, including the standards required by the United States Sarbanes-Oxley Act;
- 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 OHSAS 18001, which is subject to external certification and regular assessment;
- An external obligations register, which assists with 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.

**REPORT OF THE DIRECTORS
FOR THE YEAR ENDED 31 DECEMBER 2013**

CORPORATE GOVERNANCE STATEMENT - continued

Section C: Accountability - continued

Main Principle C3: Audit committee and auditor

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

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

R Dixon	Non-Executive Director
T E Fielden	Finance Director

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

The employee section on page 13 of the Strategic Report contains details of the Group's "speaking up" policy.

Section D: Remuneration

Main Principle D1: The level and components of remuneration

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

Main Principle D2: Procedure

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

Section E: Remuneration

Main Principle E1: Dialogue with Shareholders

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

Main Principle E2: Constructive use of the AGM

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

**REPORT OF THE DIRECTORS
FOR THE YEAR ENDED 31 DECEMBER 2013**

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors are responsible for preparing the Strategic Report, the Report of the Directors and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with International Financial Reporting Standards ("IFRS") as adopted by the European Union. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and the Group and of the profit or loss of the Group for that period.

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

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

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's and the Group's transactions and disclose with reasonable accuracy at any time the financial position of the Company and the Group and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

GOING CONCERN

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

- The Group's main subsidiaries, Northeast and Yorkshire, are stable electricity distribution businesses operating an essential public service and are regulated by GEMA. In carrying out its functions, GEMA has a statutory duty under the Electricity Act 1989 to have regard to the need to secure that licence holders are able to finance the activities, which are the subject of obligations under Part 1 of the Electricity Act 1989 (including the obligations imposed by the electricity distribution licence) or by the Utilities Act 2000;
- The Group is profitable with strong underlying cash flows. The Company, Northeast and Yorkshire hold investment grade credit ratings;
- The Group is financed by long-term borrowings with an average maturity of 13 years and has access to a £150m, five year committed revolving credit facility provided by Lloyds Bank plc, Royal Bank of Scotland plc and Abbey National Treasury Services plc; and
- No repayments of long-term debt are due until 2018.

Consequently, after making enquiries, the directors have a reasonable expectation that the Company and the Group have 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.

**REPORT OF THE DIRECTORS
FOR THE YEAR ENDED 31 DECEMBER 2013**

STATEMENT AS TO DISCLOSURE OF INFORMATION TO AUDITOR

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 auditor is 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 auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of S418 of the Companies Act 2006.

AUDITOR

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

ON BEHALF OF THE BOARD:

A handwritten signature in black ink, appearing to read 'P A Jones', is written over the printed name and title.

P A Jones
Director

16 April 2014

RESPONSIBILITY STATEMENTS OF THE DIRECTORS IN RESPECT OF THE ANNUAL REPORT AND ACCOUNTS

Each of the directors as at the date of the Annual Report, whose names and functions are set out on page 20 in the Report of the Directors confirms that, to the best of their knowledge:

- a) the accounts, prepared in accordance with applicable UK law and in conformity with IFRS, give a true and fair view of the assets, liabilities, financial position and profit of the Company and the undertakings included in the consolidation taken as a whole; and
- b) the Management Report (which is comprised of the Strategic Report and the Report of the Directors) includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties it faces.

This responsibility statement was approved by the Board of Directors on 16 April 2014 and signed on its behalf by:

A handwritten signature in black ink, appearing to read 'P A Jones', with a stylized flourish at the end.

P A Jones
President and Chief Executive Officer

16 April 2014

REPORT OF THE INDEPENDENT AUDITOR TO THE MEMBERS OF NORTHERN POWERGRID HOLDINGS COMPANY

We have audited the financial statements of Northern Powergrid Holdings Company ("the Company") for the year ended 31 December 2013, which comprise the Consolidated Statement of Profit or Loss, the Consolidated Statement of Profit or Loss and Other Comprehensive Income, the Consolidated and Company Statements of Financial Position, the Consolidated and Company Statements of Changes in Equity, the Consolidated and Company Statements of Cash Flows and the related notes 1 to 30. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. 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 a Report of the Auditor 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 auditor

As explained more fully in the Statement of Directors' Responsibilities set out on page twenty seven, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of whether the accounting policies are appropriate to the circumstances of the Company and the Group and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates made by the directors and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Strategic Report and the Report of the Directors to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the Company's and the Group's affairs as at 31 December 2013 and of the Group's profit for the year then ended;
- have been properly prepared in accordance with the requirements of the Companies Act 2006 and in accordance with IFRSs as adopted by the European Union;
- in respect of the Company have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; and
- in respect of the Group Financial Statements, have been properly prepared in accordance with Article 4 of the IAS Regulations.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Strategic Report and in the Report of the Directors for the financial year, for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception

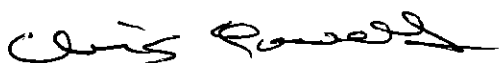
We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the Company; or
- returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements of the Company or the Group are not in agreement with the accounting records and returns; or

REPORT OF THE INDEPENDENT AUDITOR TO THE MEMBERS OF NORTHERN POWERGRID HOLDINGS COMPANY

Matters on which we are required to report by exception - continued

- the financial statements of the Company or the Group are not in agreement with the accounting records and returns;
or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.



Christopher Powell FCA (Senior Statutory Auditor)
for and on behalf of Deloitte LLP
Newcastle upon Tyne

Date: 28 April 2014

**CONSOLIDATED STATEMENT OF PROFIT OR LOSS
FOR THE YEAR ENDED 31 DECEMBER 2013**

		2013	2012
		£'000	as restated £'000
	Notes		
CONTINUING OPERATIONS			
Revenue	3	722,015	696,106
Cost of sales		<u>(56,645)</u>	<u>(46,134)</u>
GROSS PROFIT		655,370	649,972
Operating expenses	10	<u>(298,989)</u>	<u>(279,836)</u>
OPERATING PROFIT		366,381	370,136
Other gains		759	637
Finance costs	5	<u>(87,519)</u>	<u>(88,237)</u>
Finance income	5	<u>933</u>	<u>616</u>
PROFIT BEFORE INCOME TAX	6	280,554	283,152
Income tax	7	<u>(19,610)</u>	<u>(19,948)</u>
PROFIT FOR THE YEAR		<u>260,944</u>	<u>263,204</u>
Profit attributable to:			
Owners of the parent		258,332	260,572
Non-controlling interests		<u>2,612</u>	<u>2,632</u>
		<u>260,944</u>	<u>263,204</u>

**CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2013**

	2013	2012 as restated
	£'000	£'000
PROFIT FOR THE YEAR	260,944	263,204
OTHER COMPREHENSIVE INCOME		
Items that will not be reclassified subsequently to profit or loss:		
Employee benefit obligation	(8,700)	(59,700)
Income tax relating to item of other comprehensive income	(4,275)	9,980
Items that may be reclassified subsequently to profit or loss:		
Exchange difference on translation of foreign operations	(3,619)	(278)
Purchase of minority interest	<u>134</u>	<u>-</u>
OTHER COMPREHENSIVE INCOME FOR THE YEAR, NET OF INCOME TAX	<u>(16,460)</u>	<u>(49,998)</u>
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	<u>244,484</u>	<u>213,206</u>
Total comprehensive income attributable to:		
Owners of the parent	241,738	210,574
Non-controlling interests	<u>2,746</u>	<u>2,632</u>
	<u>244,484</u>	<u>213,206</u>

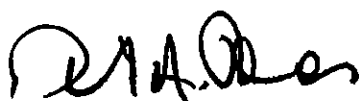
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
31 DECEMBER 2013

		2013	2012
		£'000	as restated £'000
	Notes		
ASSETS			
NON-CURRENT ASSETS			
Goodwill	12	248,843	248,843
Intangible assets	13	25,526	15,268
Property, plant and equipment	14	4,466,148	4,154,892
Investments	15	5,692	3,325
Trade and other receivables	18	6,081	4,658
		<u>4,752,290</u>	<u>4,426,986</u>
CURRENT ASSETS			
Inventories	17	10,648	11,009
Trade and other receivables	18	109,484	134,273
Cash and cash equivalents	19	5,064	54,070
		<u>125,196</u>	<u>199,352</u>
TOTAL ASSETS		<u>4,877,486</u>	<u>4,626,338</u>
EQUITY			
SHAREHOLDERS' EQUITY			
Called up share capital	21	354,550	354,550
Share premium	22	(810)	(810)
Other reserves	22	(3,926)	(307)
Retained earnings	22	1,191,932	946,575
		<u>1,541,746</u>	<u>1,300,008</u>
Non-controlling interests	20	22,088	19,342
TOTAL EQUITY		<u>1,563,834</u>	<u>1,319,350</u>

CONSOLIDATED STATEMENT OF FINANCIAL POSITION - continued
31 DECEMBER 2013

		2013	2012
		£'000	as restated £'000
LIABILITIES			
NON-CURRENT LIABILITIES			
Trade and other payables	23	1,182,568	1,151,216
Borrowings	24	1,499,770	1,503,992
Pension liability	27	10,600	36,500
Deferred tax	26	256,779	288,983
Provisions	25	4,704	4,938
		<u>2,954,421</u>	<u>2,985,629</u>
CURRENT LIABILITIES			
Trade and other payables	23	226,686	247,896
Borrowings	24	112,306	49,217
Tax payable		17,388	21,225
Provisions	25	2,851	3,021
		<u>359,231</u>	<u>321,359</u>
TOTAL LIABILITIES		<u>3,313,652</u>	<u>3,306,988</u>
TOTAL EQUITY AND LIABILITIES		<u>4,877,486</u>	<u>4,626,338</u>

The financial statements were approved by the Board of Directors on 16 April 2014 and were signed on its behalf by:



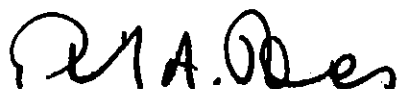
P A Jones
Director

NORTHERN POWERGRID HOLDINGS COMPANY (REGISTERED NUMBER: 03476201)

**COMPANY STATEMENT OF FINANCIAL POSITION
31 DECEMBER 2013**

	Notes	2013 £'000	2012 £'000
ASSETS			
NON-CURRENT ASSETS			
Investments	15	376,289	376,289
Loans and other financial assets	16	<u>264,158</u>	<u>264,158</u>
		<u>640,447</u>	<u>640,447</u>
CURRENT ASSETS			
Trade and other receivables	18	<u>101</u>	<u>101</u>
TOTAL ASSETS		<u>640,548</u>	<u>640,548</u>
EQUITY			
SHAREHOLDERS' EQUITY			
Called up share capital	21	354,550	354,550
Retained earnings	22	<u>75,377</u>	<u>72,826</u>
TOTAL EQUITY		<u>429,927</u>	<u>427,376</u>
LIABILITIES			
NON-CURRENT LIABILITIES			
Borrowings	24	<u>194,546</u>	<u>194,137</u>
CURRENT LIABILITIES			
Trade and other payables	23	468	429
Borrowings	24	15,160	18,507
Tax payable		<u>447</u>	<u>99</u>
		<u>16,075</u>	<u>19,035</u>
TOTAL LIABILITIES		<u>210,621</u>	<u>213,172</u>
TOTAL EQUITY AND LIABILITIES		<u>640,548</u>	<u>640,548</u>

The financial statements were approved by the Board of Directors on 16 April 2014 and were signed on its behalf by:



P A Jones
Director

**CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2013**

	Called up share capital £'000	Retained earnings £'000	Share premium £'000	Other reserves £'000
Balance at 1 January 2012 (previously reported)	354,550	897,346	(810)	(29)
Prior year adjustment	-	(161,550)	-	-
Balance at 1 January 2012 (as restated)	354,550	735,796	(810)	(29)
Changes in equity				
Movement in merger reserve	-	(73)	-	-
Foreign exchange translation adjustment	-	-	-	(278)
Profit for the year (previously reported)	-	264,640	-	-
Profit for the year (prior year adjustment)	-	(4,068)	-	-
Other comprehensive income (prior year adjustment)	-	(49,720)	-	-
Balance at 31 December 2012 (as restated)	354,550	946,575	(810)	(307)
Changes in equity				
Foreign exchange translation adjustment	-	-	-	(3,619)
Profit for the year	-	258,332	-	-
Other comprehensive income	-	(12,975)	-	-
Acquisition of minority interest	-	-	-	-
Balance at 31 December 2013	354,550	1,191,932	(810)	(3,926)
	Merger reserve £'000	Total £'000	Non-controlling interests £'000	Total equity £'000
Balance at 1 January 2012 (previously reported)	(73)	1,250,984	16,710	1,267,694
Prior year adjustment	-	(161,550)	-	(161,550)
Balance at 1 January 2012 (as restated)	(73)	1,089,434	16,710	1,106,144
Changes in equity				
Movement in merger reserve	73	-	-	-
Foreign exchange translation adjustment	-	(278)	-	(278)
Profit for the year (previously reported)	-	264,640	2,663	267,303
Profit for the year (prior year adjustment)	-	(4,068)	(31)	(4,099)
Other comprehensive income (prior year adjustment)	-	(49,720)	-	(49,720)
Balance at 31 December 2012	-	1,300,008	19,342	1,319,350
Changes in equity				
Foreign exchange translation adjustment	-	(3,619)	-	(3,619)
Profit for the year (previously reported)	-	258,332	2,612	260,944
Other comprehensive income	-	(12,975)	-	(12,975)
Acquisition of minority interest	-	-	134	134
Balance at 31 December 2013	-	1,541,746	22,088	1,563,834

COMPANY STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2013

	Called up share capital £'000	Retained earnings £'000	Total equity £'000
Balance at 1 January 2012	354,550	70,375	424,925
Changes in equity			
Total comprehensive income	-	2,451	2,451
Balance at 31 December 2012	354,550	72,826	427,376
Changes in equity			
Total comprehensive income	-	2,551	2,551
Balance at 31 December 2013	354,550	75,377	429,927

**CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2013**

		2013	2012
		£'000	as restated £'000
	Notes		
Cash flows from operating activities			
Cash generated from operations	29	448,064	422,052
Interest paid		(96,132)	(98,028)
Dividends received		187	-
Interest received		274	282
Tax paid		<u>(58,822)</u>	<u>(59,790)</u>
Net cash from operating activities		<u>293,571</u>	<u>246,516</u>
Cash flows from investing activities			
Purchase of intangible fixed assets		(18,135)	(9,444)
Purchase of tangible fixed assets		(456,681)	(380,320)
Proceeds from sale of assets		759	653
Dividends received from joint ventures		405	334
Investment in associate		(2,300)	-
Receipt of customer contributions		<u>71,553</u>	<u>97,002</u>
Net cash used in investing activities		<u>(404,399)</u>	<u>(291,775)</u>
Cash flows from financing activities			
New loans in year		61,822	147,800
Loan repayments in year		<u>-</u>	<u>(80,006)</u>
Net cash from financing activities		<u>61,822</u>	<u>67,794</u>
(Decrease)/increase in cash and cash equivalents		(49,006)	40,535
Cash and cash equivalents at beginning of year		<u>54,070</u>	<u>13,535</u>
Cash and cash equivalents at end of year		<u><u>5,064</u></u>	<u><u>54,070</u></u>

**COMPANY STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2013**

		2013 £'000	2012 £'000
	Notes		
Cash flows from operating activities			
Cash generated from operations	29	16	48
Finance costs paid		(14,767)	(14,840)
Interest received		18,491	18,491
Tax paid		<u>(393)</u>	<u>(818)</u>
Net cash from operating activities		<u>3,347</u>	<u>2,881</u>
 Cash flows from financing activities			
Loan repayments in year		<u>(3,347)</u>	<u>(2,881)</u>
Net cash used in financing activities		<u>(3,347)</u>	<u>(2,881)</u>
 Movement in cash and cash equivalents		-	-
 Cash and cash equivalents at beginning of year		<u>-</u>	<u>-</u>
 Cash and cash equivalents at end of year		<u><u>-</u></u>	<u><u>-</u></u>

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2013**

1. GENERAL INFORMATION

Northern Powergrid Holdings Company (the "Company") is a company originally incorporated in England and Wales under the Companies Act 1985. 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 Strategic Report.

2. ACCOUNTING POLICIES

Accounting convention and basis of preparation

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). These financial statements have also been prepared in accordance with IFRSs as adopted by the European Union, and with those parts of the Companies Act 2006 (the "Act") that are applicable to companies reporting under IFRS. The parent company's financial statements have also been prepared in accordance with IFRS, as applied in accordance with the provisions of the Act. The directors have taken advantage of the exemption offered by Section 408 of the Act not to present a separate statement of profit or loss for the parent company. The financial statements have been prepared under the historical cost convention. A summary of the more important group accounting policies is set out below.

Going concern

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

Judgements in applying accounting policies and key sources of estimation uncertainty

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

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

- The estimation of useful economic lives for property, plant and equipment;
- The split of operating and capital expenditure and the allocation of overheads to capital projects;
- Assumptions used when evaluating long-term pension plan assets and liabilities;
- Assumptions used when evaluating construction contracts; and
- Assumptions used when evaluating commercial reserves of oil and gas.

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.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries) made up to 31 December each year. Control is achieved where the Company has the power to govern the financial and operating policies of an investee company so as to obtain benefits from its activities.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

2. ACCOUNTING POLICIES - continued

Adoption of new or revised standards

The Group has applied IAS 19 Employee Benefits (as revised in 2011) and the related consequential amendments for the first time in 2013.

IAS 19 (as revised in 2011) changes the accounting for defined benefit plans and termination benefits. The most significant change relates to the accounting for changes in defined benefit obligations and plan assets. The amendments require the recognition of changes in defined benefit obligations and in the fair value of plan assets when they occur and hence eliminate the 'corridor approach' permitted under the previous version of IAS 19 and accelerate the recognition of past service costs. All actuarial gains and losses are recognised immediately through other comprehensive income in order for the net pension asset or liability recognised in the consolidated statement of financial position to reflect the full value of the plan deficit or surplus. Furthermore, the interest cost and expected return on plan assets used in the previous version of IAS 19 are replaced with a 'net interest' amount under IAS 19 (as revised in 2011), which is calculated by applying the discount rate to the net defined benefit liability or asset. These changes have had an impact on the amounts recognised in profit or loss and other comprehensive income in prior years (see the tables below for details). In addition, IAS 19 (as revised in 2011) introduces certain changes in the presentation of the defined benefit cost including extensive disclosures.

Specific transitional provisions are applicable to the first-time application of IAS 19 (as revised in 2011). The Group has applied the relevant transitional provisions and restated the comparative amounts on a retrospective basis (see the tables below for details).

Impact on profit/(loss) for the year of the application of IAS 19 (as revised in 2011):

	2012 as restated £m
Increase in administrative expenses	(4.6)
Decrease in income tax charge	0.5
	<u>(4.1)</u>
Decrease in profit for the year	<u>(4.1)</u>

Impact on other comprehensive income for the year of the application of IAS 19 (as revised in 2011):

	2013 £m	2012 as restated £m
Increase in re-measurement of defined benefit obligation	8.7	59.7
Increase/(decrease) in income tax relating to items of other comprehensive income	4.3	(10.0)
	<u>13.0</u>	<u>49.7</u>
Decrease in other comprehensive income for the year	<u>13.0</u>	<u>49.7</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

2. ACCOUNTING POLICIES - continued

Impact on assets, liabilities and equity as at 1 January 2012 of the application of IAS 19 (as revised in 2011):

	1 January 2012 (as previously reported) £m	IAS 19 adjustments £m	1 January 2012 (as restated) £m
<u>Assets</u>			
Pension asset	201.8	(201.8)	-
<u>Equity</u>			
Retained earnings	897.3	(161.5)	735.8
<u>Liabilities</u>			
Pension liability	1.4	13.6	15.0
Deferred tax	388.9	(53.9)	335.0

Impact on assets, liabilities and equity as at 31 December 2012 of the application of IAS 19 (as revised in 2011):

	31 December 2012 (as previously reported) £m	IAS 19 adjustments £m	31 December 2012 (as restated) £m
<u>Assets</u>			
Property, plant and equipment	4,153.6	1.3	4,154.9
Pension asset	244.5	(244.5)	-
<u>Equity</u>			
Retained earnings	1,161.9	(215.4)	946.5
<u>Liabilities</u>			
Pension liability	1.7	36.5	38.2
Deferred tax	353.3	(64.3)	289.0

IFRS 11 replaces IAS 31 - Interests in Joint Ventures. IFRS 11 deals with how a joint arrangement, in respect of which two or more parties have joint control, should be classified and accounted for. Under IFRS 11, there are only two types of joint arrangements - joint operations and joint ventures. Previously IAS 31 contemplated three types of joint arrangements - jointly controlled entities, jointly controlled operations and jointly controlled assets. The classification of joint arrangements under IAS 31 was primarily determined based on the legal form of the arrangement. Under IFRS 11, classification is determined based on the rights and obligations of the parties to the joint arrangement.

The directors reviewed and assessed the classification of the Group's investments in joint arrangements in accordance with the requirements of IFRS 11. The directors concluded that the Group's investment in Vehicle Lease and Service Limited, which was classified as a jointly controlled entity under IAS 31 and was accounted for using the equity method, should be classified as a joint venture under IFRS 11 and continue to be accounted for using the equity method. Consequently, no change in accounting is required.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013**

2. ACCOUNTING POLICIES - continued

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 Group's distribution network, amortisation of customer contributions 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 Group's distribution network include estimates of the units distributed. The estimated usage is based on historic data, judgment and assumptions. Revenues are gradually adjusted to reflect actual usage in the period during which actual meter readings are obtained.

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

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

Revenue from the sale of gas is measured at the fair value of the consideration receivable, principally from the Group's share of production from its field interests, net of value added tax.

Income from credit sale charges is apportioned in the statement of profit or loss over the period of the sales agreements.

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.

Construction contracts

Where the outcome of a construction contract can be estimated reliably, revenue and costs are recognised by reference to the stage of completion of the contract activity at the statement of financial position date. This is normally measured by the proportion that contract costs incurred for work performed to date bear to the estimated total contract costs, except where this would not be representative of the stage of completion. Variations in contract work, claims and incentive payments are included to the extent that they have been agreed with the customer.

Where the outcome of a construction contract cannot be estimated reliably, revenue in respect of that contract is recognised to the extent of the costs incurred where it is probable they will be recovered. Contract costs are recognised as expenses in the period in which they are incurred. When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately.

Operating profit

Operating profit is stated before profit on disposals, investment income and finance costs.

Software development costs

Costs in respect of major developments are capitalised and amortised over the expected life of the software. Capitalised software costs that are not an integral part of the related hardware are included in intangible assets on the statement of financial position and amortised over the expected life of the software of up to 15 years.

Gas joint venture operations

Exploration, development and production activities are conducted as co-licensee in joint ventures with other similar companies. The accounts reflect the relevant proportions of production, capital expenditure, operating costs and current assets and liabilities applicable to the Group's interests.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013**

2. ACCOUNTING POLICIES - continued

Oil and gas assets

Exploration and appraisal costs are accounted for on the successful efforts basis. All costs relating to licence and data acquisition, geological and geophysical activity and exploration and appraisal drilling are initially capitalised as intangible oil and gas assets pending determination of the commercial potential of the relevant oil and gas properties. Exploration costs, which are not incurred under a specific licence, are written off in the year incurred. If prospects are subsequently deemed to be unsuccessful on completion of evaluation, the associated costs are charged to the statement of profit or loss in the year in which that determination is made. If the prospects are deemed to be commercially viable, such costs are transferred to tangible oil and gas assets under property, plant and equipment.

Depreciation, depletion and amortisation for oil and gas properties is calculated on a unit-of-production basis, using the ratio of oil and gas production in the period to the estimated quantities of proven and probable reserves at the end of the period plus production in the period, on a field-by-field basis. Proven and probable reserve estimates are based on a number of underlying assumptions including oil and gas prices, future costs, oil and gas in place and reservoir performance, which are inherently uncertain. Management uses established industry techniques to generate its estimates and regularly references its estimates against those of joint venture partners or external consultants. However, the amount of reserves that will ultimately be recovered from any field cannot be known with certainty until the end of the field's life.

Where there has been a change in economic or commercial conditions that indicates a possible impairment in a field, the recoverability of the net book value relating to that field, less any provisions for decommissioning costs, is assessed by comparison with the estimated discounted future net cash flows based on management's expectations of future gas and oil prices and future costs. Any impairment identified is charged to the statement of profit or loss as additional depreciation. Where conditions giving rise to impairment subsequently reverse, the effect of the impairment charge is also reversed as a credit to the statement of profit or loss.

Commercial reserves of oil and gas

Commercial reserves used in the unit of production calculations are proven and probable reserves. Reserves are based on estimates provided by the operators.

The effects of changes in estimated costs or other factors affecting oil and gas unit of production calculations for depreciation and abandonment costs are dealt with prospectively over the estimated remaining commercial reserves of each field.

Abandonment Costs

Provisions for decommissioning costs are recorded at the present value of the expenditures expected to be required to settle the Group's future obligation, to the extent any damage has been caused to date taking risks and uncertainties into account in reaching the best estimates and, where available, operators' estimates. Assumptions, based on the current economic environment, have been made which management believes are a reasonable basis upon which to estimate the future liability.

A decommissioning asset is also established, since the future cost of decommissioning is regarded as part of the total investment to gain access to future economic benefit. The decommissioning asset is then depleted by field on a unit-of-production basis.

Provisions are reviewed at each statement of financial position date to reflect the current best estimate of the cost at present value. However, actual decommissioning costs will ultimately depend upon future market prices for the necessary decommissioning works required which will reflect market conditions at the relevant time. Furthermore, the timing of decommissioning is likely to depend on when the fields cease to produce at economically viable rates. This in turn will depend upon future oil and gas prices, which are inherently uncertain.

It is assumed that certain abandonment costs will be allowable for Petroleum Revenue Tax ("PRT") and corporation tax purposes when incurred.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

2. ACCOUNTING POLICIES - continued

Reserves

Reserves shown as "Other" on the statement of financial position are foreign currency translation reserves, primarily held in the Group's investment in the CE Gas group.

Investments

Undertakings, other than subsidiary undertakings, which the Group jointly controls, are treated as joint venture entities.

The results and assets and liabilities of joint venture entities are incorporated in these financial statements using the equity method of accounting except when classified as held for sale. Investments in joint venture entities are carried in the statement of financial position at cost as adjusted by post-acquisition changes in the Group's share of the net assets of the joint venture entities, less any impairment in the value of individual investments. Losses of the joint venture in excess of the Group's interest in those joint venture entities are not recognised.

Fixed asset investments are stated at cost less provision or amounts written off for impairment in value.

Goodwill

Goodwill arising on consolidation represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets and liabilities of a subsidiary or jointly controlled entity at the date of acquisition. Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. Goodwill which is recognised as an asset is reviewed for impairment at least annually. Any impairment is recognised immediately in the statement of profit or loss and is not subsequently reversed.

For the purpose of impairment testing, goodwill is allocated to each of the Group's cash-generating units expected to benefit from the synergies of the combination. Cash-generating units to which goodwill has been allocated are tested for impairment annually or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro-rata on the basis of the carrying amount of each asset in the unit. An impairment loss recognised for goodwill is not reversed in a subsequent year.

On disposal of a subsidiary or jointly controlled entity, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

2. ACCOUNTING POLICIES - continued

Property, plant and equipment and depreciation

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

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

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

In accordance with IFRS, the Group 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.

Financial instruments

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

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

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

2. ACCOUNTING POLICIES - continued

Fair value measurements

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

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

Financial liabilities and equity

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

Cash and cash equivalents

Cash and cash equivalents (which are presented as a single class of assets on the face of the statement of financial position) comprise cash at bank and other short-term highly liquid investments with a maturity of three months or less, which are subject to an insignificant risk of changes in value.

Inventories

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

Raw materials and goods for resale are valued at purchase cost on an average price basis.

Net realisable value is based on estimated selling price less further costs expected to be incurred to completion and costs to be incurred in marketing, selling and distribution.

Taxation

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

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

To the extent that gains or losses are recognised in other comprehensive income, tax related to those gains or losses are recognised in other comprehensive income.

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

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

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised. Deferred tax is charged or credited in the statement of profit or loss, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

2. ACCOUNTING POLICIES – continued

Taxation - continued

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Research costs

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

Other than the software development and gas licenses noted below, the Group and the Company do not carry out any other development activity that would give rise to an intangible asset.

Leases

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

Operating lease rentals are charged to the statement of profit or loss or to property, plant and equipment in equal annual amounts over the lease term.

Pensions

The Group contributes to the Northern Powergrid Group of the Electricity Supply Pension Scheme (the "Northern Powergrid Group of the ESPS"), a defined benefit scheme.

The cost of providing benefits is determined using the projected unit credit method, with actuarial valuations being carried out at each December statement of financial position date. Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions in excess of the greater of 10% of the value of the plan assets or 10% of the defined benefit obligation are spread to income over the employees' expected average remaining working lives.

Past service cost is recognised immediately, to the extent that the benefits are already vested, and otherwise is amortised on a straight-line basis over the average period until the benefits become vested.

The asset or liability recognised in the statement of financial position represents the present value of the defined benefit obligation less the fair value of the scheme assets on a bid value basis, together with adjustments for unrecognised actuarial gains and losses and past service costs. The asset or liability initially recognised is then assessed against the requirements of IFRIC 14, The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction, and adjustments made when appropriate.

The defined benefit obligation is calculated annually by an independent actuary using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the future cash outflows using yields on high quality sterling corporate bonds that have terms to maturity approximating to the terms of the related pension liability.

The key assumptions used for the actuarial valuation are based on the best estimate of the variables that will determine the ultimate cost of providing post-employment benefits and follow discussions with the actuary. The operating results are affected by the actuarial assumptions used. These assumptions include investment returns on the scheme's assets, discount rates, pay growth and increases to pensions and deferred pensions. These assumptions may differ from actual results due to changing market and economic conditions and longer or shorter lives of scheme members. Further detail is provided in Note 27.

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013**

2. ACCOUNTING POLICIES – continued

Foreign currency

Transactions in foreign currencies are recorded at the rate of exchange at the date of the transaction or, if hedged, at the forward contract rate. Monetary assets and liabilities denominated in foreign currencies at the statement of financial position date are reported at the rates of exchange prevailing at that date or, if appropriate, at the forward contract rate.

The results of overseas operations are translated at the average rates of exchange during the year and their statements of financial position at the rates ruling at the statement of financial position date. Exchange differences arising on translation of the opening net assets and results of overseas operations are reported in the statement of recognised income and expense. All other exchange differences are included in the statement of profit or loss.

Provisions

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

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

Trade receivables

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

Trade payables

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

Borrowings

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

3. SEGMENTAL REPORTING

The tables below represent the internal information provided to the President and Chief Executive Officer of the Group for the purposes of resource allocation and segmental performance appraisal.

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

Group revenue, Group profit before tax and Group net assets are analysed below:

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

3. SEGMENTAL REPORTING - continued

	Distribution 2013 £m	Other 2013 £m	Total 2013 £m
REVENUE			
External sales	680.7	41.3	722.0
Inter-segment sales	0.6	(0.6)	-
Total revenue	681.3	40.7	722.0
SEGMENT RESULTS			
Operating profit	339.4	27.0	366.4
Other gains			0.8
Finance costs			(87.5)
Finance income			0.9
Profit before tax			280.6
OTHER INFORMATION			
Capital additions	455.1	25.6	480.7
Depreciation and amortisation	143.8	15.3	159.1
Amortisation of deferred revenue	(38.5)	-	(38.5)
STATEMENT OF FINANCIAL POSITION			
Segment assets	4,507.3	355.2	4,862.5
Unallocated corporate assets			15.0
Total assets			4,877.5
Segment liabilities	(1,374.4)	(42.4)	(1,416.8)
Unallocated corporate liabilities			(1,896.9)
Total liabilities			(3,313.7)
Net assets/(liabilities) by segment	3,132.9	312.8	3,445.7
Unallocated net corporate liabilities			(1,881.9)
Total net assets			1,563.8

"Other" comprises Engineering Contracting, Hydrocarbon Exploration and business support units.

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

Unallocated corporate assets and liabilities include cash and cash equivalents (£5.1m), borrowings (£1,612.1m) and taxation (£266.6m).

External sales to RWE Npower plc in 2013 of £204.1m are included within the Distribution segment.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

3. SEGMENTAL REPORTING - continued

	Distribution 2012 £m	Other 2012 £m as restated	Total 2012 £m as restated
REVENUE			
External sales	661.9	34.2	696.1
Inter-segment sales	<u>0.6</u>	<u>(0.6)</u>	<u>-</u>
Total revenue	<u>662.5</u>	<u>33.6</u>	<u>696.1</u>
SEGMENT RESULTS			
Operating profit	<u>337.4</u>	<u>32.7</u>	370.1
Other gains			0.6
Finance costs			(88.2)
Finance income			<u>0.6</u>
Profit before tax			<u>283.1</u>
OTHER INFORMATION			
Capital additions	426.4	6.7	433.1
Depreciation and amortisation	142.1	4.5	146.6
Amortisation of deferred revenue	<u>(37.5)</u>	<u>-</u>	<u>(37.5)</u>
STATEMENT OF FINANCIAL POSITION			
Segment assets	<u>4,544.9</u>	<u>27.4</u>	4,572.3
Unallocated corporate assets			<u>54.0</u>
Total assets			<u>4,626.3</u>
Segment liabilities	<u>(1,392.5)</u>	<u>(51.1)</u>	(1,443.6)
Unallocated corporate liabilities			<u>(1,863.4)</u>
Total liabilities			<u>(3,307.0)</u>
Net assets/(liabilities) by segment	<u>3,152.4</u>	<u>(23.7)</u>	3,128.7
Unallocated net corporate liabilities			<u>(1,809.4)</u>
Total net assets			<u>1,319.3</u>

"Other" comprises Engineering Contracting, Hydrocarbon Exploration and business Support units.

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

Unallocated corporate assets and liabilities include cash and cash equivalents (£54.1m), borrowings (£1,553.2m) and taxation (£310.2m).

External sales to RWE Npower plc in 2012 of £191.4m are included within the Distribution segment.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

4. EMPLOYEES AND DIRECTORS

	2013	2012 as restated
	£'000	£'000
Salaries	108,666	103,224
Social security costs	11,546	10,228
Defined benefit pension costs	16,200	13,000
Defined contribution pension costs	<u>2,436</u>	<u>1,519</u>
	138,848	127,971
Less charged to property, plant and equipment	<u>(83,007)</u>	<u>(80,746)</u>
	<u>55,841</u>	<u>47,225</u>

The majority of the Group's employees are members of the Northern Powergrid Group of the ESPS, details of which are given in the Employee Benefit Obligations note.

The average monthly number of employees during the year was:

	2013 No.	2012 No.
Distribution	2,181	2,105
Engineering Contracting	191	180
Hydrocarbon exploration and development	15	12
Other	<u>44</u>	<u>56</u>
	<u>2,431</u>	<u>2,353</u>

The Company had no employees in the years ended 31 December 2013 and 31 December 2012.

DIRECTORS' REMUNERATION

	2013 £'000	2012 £'000
Highest Paid:		
Short-term employee benefits	417	292
Post-employment benefits	46	49
Other long-term benefits	<u>545</u>	<u>503</u>
	<u>1,008</u>	<u>844</u>
Total:		
Short-term employee benefits	607	474
Post-employment benefits	46	64
Other long-term benefits	<u>736</u>	<u>673</u>
	<u>1,389</u>	<u>1,211</u>
Directors who are a member of the defined benefit scheme	<u>3</u>	<u>3</u>
Accrued pension benefit relating to highest paid director	<u>-</u>	<u>-</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

4. EMPLOYEES AND DIRECTORS - continued

OTHER KEY PERSONNEL REMUNERATION

	2013	2012
	£'000	£'000
Total:		
Short-term employee benefits	804	864
Post-employment benefits	205	227
Other long-term benefits	<u>777</u>	<u>685</u>
	<u>1,786</u>	<u>1,776</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 Group.

5. NET FINANCE COSTS

	2013	2012
	£'000	£'000
Finance income:		
Share of profit after tax of joint venture	472	334
Dividends received	187	-
Interest receivable	<u>274</u>	<u>282</u>
	<u>933</u>	<u>616</u>
	2013	2012
	£'000	£'000
Finance costs:		
Interest payable on external borrowings	84,620	85,349
Unwinding of discount on abandonment provision	120	109
Preference dividends	<u>2,779</u>	<u>2,779</u>
	<u>87,519</u>	<u>88,237</u>
Net finance costs	<u>86,586</u>	<u>87,621</u>

During the year ended 31 December 2013, £5,841,000 of borrowing costs were capitalised (2012: £2,441,000).

6. PROFIT BEFORE INCOME TAX

The profit before income tax is stated after charging/(crediting):

	2013	2012
	£'000	£'000
Depreciation - owned assets	151,266	141,269
Profit on disposal of fixed assets	(759)	(637)
Oil & gas assets amortisation	5,706	3,301
Software development costs amortisation	2,171	2,028
Research costs	12,906	13,767
Amortisation of deferred revenue	(41,462)	(37,535)
Impairment loss on trade and other receivables	<u>288</u>	<u>278</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

6. PROFIT BEFORE INCOME TAX - continued

Analysis of auditor's remuneration is as follows:

	2013 £'000	2012 £'000
Fees payable to the Company's auditor for the audit of the Company's annual accounts	120	113
Fees payable to the Company's auditor for the audit of the Company's subsidiaries pursuant to legislation	<u>370</u>	<u>358</u>
Total audit fees	<u>490</u>	<u>471</u>
Other services	<u>194</u>	<u>226</u>
Total auditor's remuneration	<u>684</u>	<u>697</u>
	2013 £'000	2012 £'000
Fees payable to the Company's auditor for other services pursuant to legislation	<u>6</u>	<u>5</u>

7. INCOME TAX

Analysis of tax expense

	2013 £'000	2012 as restated £'000
Current tax	64,134	65,156
Deferred tax	<u>(44,524)</u>	<u>(45,208)</u>
Total tax expense in consolidated statement of profit or loss	<u>19,610</u>	<u>19,948</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

7. INCOME TAX - continued

Factors affecting the tax expense

The income tax charge for the year in the Statement of Profit or Loss is lower (2012: lower) than the standard rate of corporation tax in the UK. The difference is explained below:

	2013	2012 as restated
	£'000	£'000
Profit on ordinary activities before income tax	<u>280,554</u>	<u>283,152</u>
Profit on ordinary activities multiplied by the standard rate of corporation tax in the UK of 23.25% (2012 - 24.50%)	65,229	69,372
Effects of:		
Interest payable on non-cumulative preference shares	646	556
Tax effect of result of joint venture entities	(110)	(82)
PRT	15	437
Over provision for prior years	(2,337)	(19,307)
Effect of change in tax rates	(46,139)	(31,585)
Pension contributions recognised in Other Comprehensive Income ("OCI")	2,238	557
Other	<u>68</u>	<u>-</u>
Tax expense	<u>19,610</u>	<u>19,948</u>

Tax effects relating to effects of other comprehensive income

	2013		
	Gross £'000	Tax £'000	Net £'000
Re-measurement of net pension obligation	(8,700)	1,508	(7,192)
Pension contributions paid	-	2,238	2,238
Impact of change in tax rate	-	<u>(8,021)</u>	<u>(8,021)</u>
	<u>(8,700)</u>	<u>(4,275)</u>	<u>(12,975)</u>

	2012 as restated		
	Gross £'000	Tax £'000	Net £'000
Re-measurement of net pension obligation	(59,700)	13,731	(45,969)
Pension contributions paid	-	557	557
Impact of change in tax rate	-	<u>(4,308)</u>	<u>(4,308)</u>
	<u>(59,700)</u>	<u>9,980</u>	<u>(49,720)</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

7. INCOME TAX - continued

	2013	2012 as restated
	£'000	£'000
Tax expense comprises:		
Current tax expense:		
Corporation tax charge for the year	66,471	72,141
PRT	-	705
Over provision for prior years	<u>(2,337)</u>	<u>(7,690)</u>
Total current tax charge	64,134	65,156
Deferred tax:		
Deferred tax expenses relating to the origination and reversal of temporary differences	1,615	(13,623)
Effect of changes in tax rates	<u>(46,139)</u>	<u>(31,585)</u>
Total deferred tax charge	<u>(44,524)</u>	<u>(45,208)</u>
Tax on profit before tax	<u>19,610</u>	<u>19,948</u>

The Finance Act 2013 includes a provision that the standard rate of corporation tax in the United Kingdom will reduce from 23% to 21% from April 2014 and to 20% from April 2015. Accordingly, 20% has been applied when calculating deferred tax assets and liabilities throughout the Group as at 31 December 2013.

8. PROFIT OF PARENT COMPANY

As permitted by Section 408 of the Companies Act 2006, the statement of profit or loss of the parent company is not presented as part of these financial statements. The parent company's profit for the financial year was £2,551,000 (2012 - £2,451,000).

9. PRIOR YEAR ADJUSTMENT

Amounts due from customers for contract work:

Integrated Utility Services Limited ("IUS") is part of the Group and operates an engineering contracting business. Construction contracts arising in the normal course of business are accounted for under IAS 11 Construction Contracts. The policy allows for revenue and costs to be recognised by reference to the stage of completion of the contract activity, when the outcome of the contract can be measured reliably, at the statement of financial position date.

When contract costs incurred to date plus recognised profit less recognised losses exceed progress billings, the surplus is shown as amounts due from customers for contract work in the statement of financial position.

In prior years this has been aggregated into the inventories line in the statement of financial position and disclosed separately as work in progress within the inventories note in the notes to the financial statements. Amounts due from customers for contract work should be included within trade and other receivables rather than inventories on the face of the statement of financial position.

The 2012 balance of £4,355,000 has been restated to be included in trade and other receivables. The comparable 2013 balance is £4,329,000. Consequently, this impacts the movement in working capital in the cash flow statement. There is no impact elsewhere in the financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

10. OPERATING EXPENSES

Operating expenses comprise:

	2013 £'000	2012 as restated £'000
Distribution costs	90,324	84,056
Administrative expenses	208,665	195,780
	<u>298,989</u>	<u>279,836</u>

11. OPERATING LEASE COMMITMENTS

Group

	2013 £'000	2012 £'000
Minimum lease payments under operating leases recognised in the year	<u>11,405</u>	<u>10,674</u>

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

	2013 £'000	2012 £'000
Within one year	8,643	8,200
In the second to fifth year	23,481	23,242
After five years	<u>6,364</u>	<u>9,632</u>
	<u>38,488</u>	<u>41,074</u>

The lease commitments represent obligations in relation to property and transport facilities. The transport facilities are provided by Vehicle Lease and Service Limited, a joint venture entity.

The Company had no obligations under operating leases (2012: £nil).

12. GOODWILL

Group

	2013 £'000	2012 £'000
COST AND NET BOOK VALUE		
At 1 January and 31 December	<u>248,843</u>	<u>248,843</u>

All of the goodwill arose on the acquisition of Yorkshire Power Group Limited prior to the adoption of IFRS by the Group. In accordance with the transitional rules on first time adoption, the allocation of goodwill to cash generating units ("CGU") has not been reassessed from that used in the previous UK GAAP accounts.

The Group's distribution activities comprise two cash generating units ("CGUs") with carrying values as follows:

	2013 £m	2012 £m
Northern Powergrid (Northeast) Limited	1,431	1,304
Northern Powergrid (Yorkshire) plc (including Goodwill)	<u>2,086</u>	<u>1,946</u>
Total Distribution	<u>3,517</u>	<u>3,250</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

12. GOODWILL - continued

The carrying values of the CGUs comprise tangible and intangible assets with finite lives and are net of deferred revenues. In addition, the Northern Powergrid (Yorkshire) plc CGU includes goodwill of £248.8m (2012: £248.8m).

The Group tests goodwill annually for impairment or more frequently if there are indications that goodwill might be impaired.

The recoverable amounts of the CGUs are determined from value in use calculations. The key assumptions for the value in use calculations are those regarding the discount rates, growth rates and expected outcomes of future distribution price control reviews.

Management estimates discount rates using pre-tax rates that reflect the current market assessments of the time value of money and the risks specific to the CGUs. Growth rates are derived from the historic results and the forecasts in the most recent board approved budgets and ten-year plans. The use of the ten-year plan reflects the long-term nature of the assets and associated costs as well as the regulatory environment within which future revenue is determined. The rate used to discount the cash flows applicable to Northern Powergrid (Northeast) Limited and Northern Powergrid (Yorkshire) plc was 5.3% (2012: 5.3%) pre-tax and ignoring the impact of price inflation. This rate represents the directors' estimate of the average rate of return for the Group, incorporating some degree of out-performance against Ofgem allowances.

The forecast of cash flows for future periods is extrapolated from the last year of the plan based on an estimated growth rate of 2.6% (real ignoring the impact of projected price inflation).

The application of these assumptions did not give rise to an impairment charge in 2013 (2012: £nil).

13. INTANGIBLE ASSETS

Group

	Oil & Gas Assets £'000	Software Development Costs £'000	Totals £'000
COST			
At 1 January 2013	21,271	70,379	91,650
Additions	<u>9,360</u>	<u>8,775</u>	<u>18,135</u>
At 31 December 2013	<u>30,631</u>	<u>79,154</u>	<u>109,785</u>
AMORTISATION			
At 1 January 2013	14,578	61,804	76,382
Amortisation for year	<u>5,706</u>	<u>2,171</u>	<u>7,877</u>
At 31 December 2013	<u>20,284</u>	<u>63,975</u>	<u>84,259</u>
NET BOOK VALUE			
At 31 December 2013	<u>10,347</u>	<u>15,179</u>	<u>25,526</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

13. INTANGIBLE ASSETS - continued

	Oil & Gas Assets £'000	Software Development Costs £'000	Totals £'000
COST			
At 1 January 2012	15,843	66,363	82,206
Additions	<u>5,428</u>	<u>4,016</u>	<u>9,444</u>
At 31 December 2012	<u>21,271</u>	<u>70,379</u>	<u>91,650</u>
AMORTISATION			
At 1 January 2012	11,277	59,776	71,053
Amortisation for year	<u>3,301</u>	<u>2,028</u>	<u>5,329</u>
At 31 December 2012	<u>14,578</u>	<u>61,804</u>	<u>76,382</u>
NET BOOK VALUE			
At 31 December 2012	<u>6,693</u>	<u>8,575</u>	<u>15,268</u>

The Company had no intangible assets at 31 December 2013 or 31 December 2012.

14. PROPERTY, PLANT AND EQUIPMENT

Group	Non-operational land & buildings £'000	Distribution system £'000	Fixtures and fittings £'000	Oil & gas assets £'000	Totals £'000
COST					
At 1 January 2013	7,899	5,351,908	52,257	4,764	5,416,828
Additions	146	443,920	3,344	15,112	462,522
Disposals	<u>-</u>	<u>(21,501)</u>	<u>(287)</u>	<u>-</u>	<u>(21,788)</u>
At 31 December 2013	<u>8,045</u>	<u>5,774,327</u>	<u>55,314</u>	<u>19,876</u>	<u>5,857,562</u>
DEPRECIATION					
At 1 January 2013	2,190	1,209,107	46,418	4,221	1,261,936
Charge for year	1,160	145,900	3,447	759	151,266
Eliminated on disposal	<u>-</u>	<u>(21,501)</u>	<u>(287)</u>	<u>-</u>	<u>(21,788)</u>
At 31 December 2013	<u>3,350</u>	<u>1,333,506</u>	<u>49,578</u>	<u>4,980</u>	<u>1,391,414</u>
NET BOOK VALUE					
At 31 December 2013	<u>4,695</u>	<u>4,440,821</u>	<u>5,736</u>	<u>14,896</u>	<u>4,466,148</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

14. PROPERTY, PLANT AND EQUIPMENT - continued

	Non-operational land & buildings £'000	Distribution system £'000	Fixtures and fittings £'000	Oil & gas assets £'000	Totals £'000
COST					
At 1 January 2012	7,899	4,946,172	48,545	4,710	5,007,326
Additions (as restated)	-	419,636	4,017	54	423,707
Disposals	-	(13,900)	(305)	-	(14,205)
At 31 December 2012 (as restated)	7,899	5,351,908	52,257	4,764	5,416,828
DEPRECIATION					
At 1 January 2012	1,872	1,087,061	42,690	3,233	1,134,856
Charge for year	318	135,930	4,033	988	141,269
Eliminated on disposal	-	(13,884)	(305)	-	(14,189)
At 31 December 2012	2,190	1,209,107	46,418	4,221	1,261,936
NET BOOK VALUE					
At 31 December 2012 (as restated)	5,709	4,142,801	5,839	543	4,154,892

Group

Assets in the course of construction included above:

	Distribution system £'000	Fixtures and fittings £'000	Totals £'000
At 1 January 2013	277,137	2,718	279,855
Additions	442,903	3,387	446,290
Available for use	(365,063)	(3,387)	(368,450)
At 31 December 2013	354,977	2,718	357,695

The Group has entered into contractual commitments in relation to the future acquisition of property, plant and equipment of £82.2m (2012: £59.8m).

The net book value of the Group's non-operational land and buildings comprises:

	2013 £'000	2012 £'000
Freehold	3,103	4,059
Long leasehold	1,270	1,302
Short leasehold	322	348
	4,695	5,709

The Company had no property, plant and equipment assets as at 31 December 2013 (2012: £nil)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

15. INVESTMENTS

	Group			Company	
	Share of joint Venture's net assets	Share of associate's net assets	Shares in other undertakings	Total	Share in subsidiary undertakings
	£'000	£'000	£'000	£'000	£'000
At 1 January 2013	3,304	-	21	3,325	376,289
Acquisitions	-	2,300	-	2,300	-
Movement	67	-	-	67	-
At 31 December 2013	<u>3,371</u>	<u>2,300</u>	<u>21</u>	<u>5,692</u>	<u>376,289</u>

Details of the principal investments of the Group at 31 December 2013 are listed below:

Principal subsidiary undertakings held by the Company:

Name of company	Holding of shares	Proportion of voting rights and shares held	Nature of business
CE Electric UK Holdings	354,550,312 at £1	99%	Holding company
Yorkshire Power Group Limited	23,100,001 at £1	5.25%	Holding company

Held by CE Electric UK Holdings and its Subsidiaries:

Name of company	Holding of shares	Proportion of voting rights and shares held	Nature of business
CalEnergy Gas Limited	2,682,373 at £1	100%	Hydrocarbon exploration and development
CalEnergy Gas (Holdings) Limited	36,000,000 at £1	100%	Holding company
CalEnergy Resources Limited	17,298,755 at £1	100%	Holding company
CalEnergy Resources (Australia) Limited	1 at £1	100%	Hydrocarbon exploration and development
CE Electric (Ireland) Limited	2 at 1 Euro	100%	Non-trading company
CE UK Gas Holdings Limited	36,000,001 at £1	100%	Holding company
Integrated Utility Services Limited	3,103,000 at £1	100%	Engineering contracting services
Integrated Utility Services Limited (registered in Eire)	10,000 at 1.27 Euro	100%	Engineering contracting services
NewGen Drilling Pty Limited (registered in Australia)	24,830,490 at \$1	99.2%	Hydrocarbon exploration and development
Northern Electric & Gas Limited	84,785,000 at £1	100%	Non-trading company
Northern Electric plc (ordinary shares)	127,689,809 at 56 12/23p	100%	Holding company
Northern Electric plc (preference shares)	77,188,706 at 1p	69.1%	Holding company
Northern Electric Properties Limited	32,207,100 at £1	100%	Property management company
Northern Electric Finance plc	50,000 at £1	100%	Finance company
Northern Powergrid Limited	405,000,000 at £1	100%	Holding company

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

15. INVESTMENTS - continued

Held by CE Electric UK Holdings and its Subsidiaries:

Name of company	Holding of shares	Proportion of voting rights and shares held	Nature of business
Northern Powergrid (Northeast) Limited	200,000,100 at £1	100%	Distribution of electricity
Northern Powergrid (Yorkshire) plc	290,000,000 at £1	100%	Distribution of electricity
Northern Transport Finance Limited	7,000,000 at £1	100%	Car finance company
Yorkshire Electricity Group plc	159,270,954 at 68 2/11p	100%	Holding company
Yorkshire Power Finance Limited (registered in the Cayman Islands)	2,000 at \$1	100%	Finance company
Yorkshire Power Group Limited	416,900,001 at £1	94.75%	Holding company

Joint Venture Entities Held by CE Electric UK Holdings and its Subsidiaries:

Name of company	Holding of shares	Proportion of voting rights and shares held	Nature of business
Vehicle Lease and Service Limited	950,000 at £1	50%	Transport Services

Associate Entities Held by CE Electric UK Holdings and its Subsidiaries:

Name of company	Holding of shares	Proportion of voting rights and shares held	Nature of business
Baltic Gas Sp z o.o. Wspolnicy Spolka Komandytowa (registered in Poland)	22,050 at PLN50	49%	Hydrocarbon exploration and development

The above companies are registered in England and Wales except where indicated.

Interest in Joint venture

Summarised financial information in respect of the Group's joint venture is set out below:

	2013 £'000	2012 £'000
Long-term assets	17,735	18,067
Current assets	15,425	14,562
Long-term liabilities	(16,093)	(16,104)
Current liabilities	(10,325)	(9,917)
Net assets	<u>6,742</u>	<u>6,608</u>
Group's share of joint venture's net assets	<u>3,371</u>	<u>3,304</u>
Revenue	<u>15,680</u>	<u>15,219</u>
Profit for the year	<u>944</u>	<u>668</u>
Group's share of joint venture's profit for the year	<u>472</u>	<u>334</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

16. LOANS AND OTHER FINANCIAL ASSETS**Company**

	Book Value		Fair Value	
	2013	2012	2013	2012
	£'000	£'000	£'000	£'000
Amounts owed by subsidiary undertakings	<u>264,158</u>	<u>264,158</u>	<u>321,384</u>	<u>347,906</u>

The directors' estimate of the fair value is calculated by discounting the future cash flows at the market rate at the statement of financial position date. The valuation of assets set out above is based on Level 1 inputs. The Company's maximum risk exposure is the book value of these debts, which are not past due at the statement of financial position date. The directors do not consider there to be any indicators that these debts require impairment.

17. INVENTORIES

	Group	
	2013	2012
	£'000	as restated £'000
Stocks	9,697	10,456
Work-in-progress	340	97
Assets held for sale	<u>611</u>	<u>456</u>
	<u>10,648</u>	<u>11,009</u>

The Company had no inventories at 31 December 2013 (2012 - £nil).

18. TRADE AND OTHER RECEIVABLES

	Group		Company	
	2013	2012	2013	2012
	£'000	as restated £'000	£'000	£'000
Current:				
Distribution use of system receivable	77,267	106,615	-	-
Construction contract customers	6,567	4,645	-	-
Amounts owed from Group undertakings	4,329	4,355	-	-
Amounts receivable in respect of finance leases	3,683	3,544	-	-
Other debtors	87	772	-	-
Amounts receivable for sale of goods or services	5,098	1,543	-	-
Current petroleum revenue tax asset	353	1,457	-	-
Prepayments and accrued income	<u>12,100</u>	<u>11,342</u>	<u>101</u>	<u>101</u>
	<u>109,484</u>	<u>134,273</u>	<u>101</u>	<u>101</u>
Non-current:				
Amounts receivable in respect of finance leases	<u>6,081</u>	<u>4,658</u>	<u>-</u>	<u>-</u>
Aggregate amounts	<u>115,565</u>	<u>138,931</u>	<u>101</u>	<u>101</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

18. TRADE AND OTHER RECEIVABLES - continued

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

Distribution use of system receivables

The customers served by the Group's distribution networks are supplied predominantly by a small number of electricity supply businesses with RWE NPower plc accounting for approximately 27% of distribution revenues in 2013 (2012: 28%). 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 £133,000 as at 31 December 2013 (2012: £92,000).

Ofgem has indicated that, provided the Group 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 Group's use of system ("UoS") receivables are debtors with a carrying value of £nil, which have been placed into administration and have therefore been provided in full at the year-end (2012: £nil).

Construction contract customers

The average credit period on construction contracts is 30 days. Interest is not generally charged on construction contracts paid after the due date. The Group has provided fully for all receivables over one year for UK Contracting debts and all receivables over six months for Multi-Utility debts. Trade receivables between 30 days and these predetermined provision dates are provided for based on estimated irrecoverable amounts, determined by reference to past default experience.

Included in the Group's construction contracts balance are debtors with a carrying amount of £2,261,000 (2012: £1,486,000), which are past due at the reporting date for which the Group has provided for an irrecoverable amount of £155,000 (2012: £27,000) based on past experience. The Group does not hold any collateral over these balances. The average age of these receivables is 70 days (2012: 66 days).

Included in the Group's construction contracts balance are debtors with a carrying amount of £nil (2012: £nil) which are past due at the reporting date for which the Group has not provided as there has not been a significant change in credit quality and the amounts are still considered recoverable. The Group does not hold any collateral over these balances. The average age of these receivables is 45 days (2012: 45 days).

Amounts due from customers for contract work

Contracts in progress at statement of financial position date:

	2013	2012
		as restated
	£'000	£'000
Contract costs incurred plus recognised profits less recognised losses to date	37,652	29,520
Less: progress billings	(33,323)	(25,165)
Amount due from customers	<u>4,329</u>	<u>4,355</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

18. TRADE AND OTHER RECEIVABLES - continued

At 31 December 2013, retentions held by customers for contract work amounted to £0.8m (2012: £0.4m).

Advances received from customers for contract work amounted to £nil (2012: £nil)

The Company had no construction contracts at 31 December 2013 (2012: £nil).

Finance lease receivables

	Minimum lease payments		Present value	
	2013 £'000	2012 £'000	2013 £'000	2012 £'000
Amounts receivable under finance leases:				
Within one year	4,218	3,918	3,683	3,544
In the second to fifth years inclusive	<u>6,520</u>	<u>4,949</u>	<u>6,081</u>	<u>4,658</u>
	10,738	8,867	9,764	8,202
Less: unearned finance income	<u>(974)</u>	<u>(665)</u>	<u>-</u>	<u>-</u>
	<u><u>9,764</u></u>	<u><u>8,202</u></u>	<u><u>9,764</u></u>	<u><u>8,202</u></u>

Northern Transport Finance Limited), a wholly-owned subsidiary, enters into credit finance arrangements for motor vehicles with employees in the Group. All agreements are denominated in sterling. The term of the finance agreements is predominantly three years.

The interest rate inherent in the agreements is fixed at the contract date for all of the term of the agreement. The average effective interest rate contracted is approximately 6.5% (2012: 6.5%) per annum. None of these debts are past due and there are no indicators of impairment. The directors consider the carrying value of finance lease receivables approximates their fair value. The maximum risk exposure is the book value of these receivables, less the residual value of the leased vehicles.

Amounts receivable from sale of goods and services

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

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

Included in the Group's amounts receivable for goods and services balance are debtors with a carrying amount of £2,222,000 (2012: £1,345,000) which are past due at the reporting date and for which the Group has provided an irrecoverable amount of £746,000 (2012: £646,000) based on past experience. The Group does not hold any collateral over these balances. The average age of these receivables is 417 days (2012: 461 days).

Included in the Group's amounts receivable for goods and services balance are debtors with a carrying amount of £958,000 (2012: £768,000). These amounts are past due at the reporting date and the Group 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 Group does not hold any collateral over these balances. The average age of these receivables is 64 days (2012: 59 days).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

18. TRADE AND OTHER RECEIVABLES - continued

Amounts receivable from sale of goods and services - continued

Ageing of past due but not impaired receivables:

	2013	2012
	£'000	£'000
30-60 days	699	581
60-120 days	172	147
120-210 days	87	40
Total	<u>958</u>	<u>768</u>

Movement in the allowance for doubtful debts

	2013	2012
	£'000	£'000
At 1 January	673	631
Amounts utilised/written off in the year	(288)	(247)
Amounts recognised in income statement	<u>515</u>	<u>289</u>
At 31 December	<u>900</u>	<u>673</u>

In determining the recoverability of the trade and other receivables, the Group 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 £342,000 (2012: £412,000), 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.

Categories of financial assets

	2013	2012
	£'000	as restated £'000
Group:		
Cash and bank balances	5,064	54,070
Designated as fair value through the profit and loss	5,692	3,325
Loans and receivables at amortised cost	<u>103,112</u>	<u>126,132</u>
Total financial assets	<u>113,868</u>	<u>183,527</u>
 Non-current assets	 4,740,517	 4,419,003
Inventories	10,648	11,009
Other tax assets	353	1,457
Prepayments and accrued income	<u>12,100</u>	<u>11,342</u>
Total non-financial assets	<u>4,763,618</u>	<u>4,442,811</u>
Total assets	<u>4,877,486</u>	<u>4,626,338</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

18. TRADE AND OTHER RECEIVABLES - continued

Categories of financial assets - continued

	2013	2012
Company:	£'000	£'000
Receivables	101	101
Loans and receivables at amortised cost	<u>264,158</u>	<u>264,158</u>
Total financial assets	<u>264,259</u>	<u>264,259</u>
Investments held in subsidiaries and joint ventures	<u>376,289</u>	<u>376,289</u>
Total non-financial assets	<u>376,289</u>	<u>376,289</u>
Total assets	<u>640,548</u>	<u>640,548</u>

19. CASH AND CASH EQUIVALENTS

	Group		Company	
	2013	2012	2013	2012
	£'000	£'000	£'000	£'000
Short-term deposits	2,195	862	-	-
Cash at bank and in hand	<u>2,869</u>	<u>53,208</u>	<u>-</u>	<u>-</u>
	<u>5,064</u>	<u>54,070</u>	<u>-</u>	<u>-</u>

Cash and cash equivalents have a maturity of less than three months, are readily convertible to cash and are subject to an insignificant risk of changes in value. The carrying amount of these assets approximates their fair value.

20. NON-CONTROLLING INTERESTS

	2013	2012
	£'000	as restated £'000
At 1 January	19,342	16,710
Acquisition of NewGen Drilling Pty Limited	134	-
Share of profit on ordinary activities after tax	<u>2,612</u>	<u>2,632</u>
At 31 December	<u>22,088</u>	<u>19,342</u>

21. CALLED UP SHARE CAPITAL

	2013	2012
	No.	No.
Ordinary shares at £1 each		
Allotted, called up and fully paid	<u>354,550,000</u>	<u>354,550,000</u>
	2013	2012
	£'000	£'000
Ordinary shares at £1 each		
Allotted, called up and fully paid	<u>354,550</u>	<u>354,550</u>

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

22. RESERVES

Group	Retained earnings £'000	Share premium £'000	Other reserves £'000	Totals £'000
At 1 January 2013	946,575	(810)	(307)	945,458
Profit for the year	258,332	-	-	258,332
Movements on pension reserve	(12,975)	-	-	(12,975)
Movements on foreign exchange	-	-	(3,619)	(3,619)
At 31 December 2013	<u>1,191,932</u>	<u>(810)</u>	<u>(3,926)</u>	<u>1,187,196</u>

	Retained earnings £'000	Share premium £'000	Other reserves £'000	Merger reserve £'000	Totals £'000
At 1 January 2012 (as restated)	735,796	(810)	(29)	(73)	734,884
Profit for the year (as restated)	260,572	-	-	-	260,572
Movements on pension reserve (as restated)	(49,720)	-	-	-	(49,720)
Movements on foreign exchange	-	-	(278)	-	(278)
Movements on merger reserve	(73)	-	-	73	-
At 31 December 2012 (as restated)	<u>946,575</u>	<u>(810)</u>	<u>(307)</u>	<u>-</u>	<u>945,458</u>

Company	Retained earnings £'000
At 1 January 2013	72,826
Profit for the year	<u>2,551</u>
At 31 December 2013	<u>75,377</u>

	Retained earnings £'000
At 1 January 2012	70,375
Profit for the year	<u>2,451</u>
At 31 December 2012	<u>72,826</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

23. TRADE AND OTHER PAYABLES

	Group		Company	
	2013	2012	2013	2012
	£'000	£'000	£'000	£'000
Current:				
Payments on account	65,313	69,768	-	-
Trade creditors	11,388	9,525	-	-
Amounts owed to joint venture entities	1,082	1,028	-	-
Social security and other taxes	6,694	14,611	-	-
Other creditors	15,728	15,578	-	-
Amounts owed to parent undertakings	468	429	468	429
Deferred revenue	47,469	42,386	-	-
Accrued expenses	78,544	94,571	-	-
	<u>226,686</u>	<u>247,896</u>	<u>468</u>	<u>429</u>
Non-current:				
Deferred revenue	<u>1,182,568</u>	<u>1,151,216</u>	-	-
	<u>1,182,568</u>	<u>1,151,216</u>	-	-
Aggregate amounts	<u>1,409,254</u>	<u>1,399,112</u>	<u>468</u>	<u>429</u>

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

23. TRADE AND OTHER PAYABLES - continued

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

Group

	Less than 3 months £'000	3 months to 1 year £'000	1 to 5 years £'000	5+ years £'000	Total £'000
2013:					
Non-interest bearing	113,904	-	-	-	113,904
Variable interest rate liability	63,948	-	-	-	63,948
Fixed interest rate liability	<u>23,531</u>	<u>67,565</u>	<u>404,383</u>	<u>2,089,625</u>	<u>2,585,104</u>
	<u>201,383</u>	<u>67,565</u>	<u>404,383</u>	<u>2,089,625</u>	<u>2,762,956</u>
2012:					
Non-interest bearing	137,204	-	-	-	137,204
Variable interest rate liability	2,126	-	-	-	2,126
Fixed interest rate liability	<u>23,533</u>	<u>68,616</u>	<u>368,597</u>	<u>2,247,792</u>	<u>2,708,538</u>
	<u>162,863</u>	<u>68,616</u>	<u>368,597</u>	<u>2,247,792</u>	<u>2,847,868</u>

Company

	Less than 3 months £'000	3 months to 1 year £'000	1 to 5 years £'000	5+ years £'000	Total £'000
2013:					
Non-interest bearing	468	-	-	-	468
Variable interest rate liability	14,516	-	-	-	14,516
Fixed interest rate liability	<u>-</u>	<u>14,500</u>	<u>58,000</u>	<u>258,000</u>	<u>330,500</u>
	<u>14,984</u>	<u>14,500</u>	<u>58,000</u>	<u>258,000</u>	<u>345,484</u>
2012:					
Non-interest bearing	429	-	-	-	429
Variable interest rate liability	17,948	-	-	-	17,948
Fixed interest rate liability	<u>-</u>	<u>14,500</u>	<u>58,000</u>	<u>272,500</u>	<u>345,000</u>
	<u>18,377</u>	<u>14,500</u>	<u>58,000</u>	<u>272,500</u>	<u>363,377</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

23. TRADE AND OTHER PAYABLES - continued

Categories of financial liabilities

Group	2013 £'000	2012 £'000
Loans and payables at amortised cost	<u>(1,640,742)</u>	<u>(1,579,769)</u>
Total financial liabilities	<u>(1,640,742)</u>	<u>(1,579,769)</u>
Payments received on account	(65,313)	(69,768)
Income tax liabilities	(274,167)	(310,208)
Other taxes and social security	(6,694)	(14,611)
Accruals	(78,544)	(94,571)
Deferred revenue	(1,230,037)	(1,193,602)
Pension liability	(10,600)	(36,500)
Provisions	<u>(7,555)</u>	<u>(7,959)</u>
Total non-financial liabilities	<u>(1,672,910)</u>	<u>(1,727,219)</u>
Total liabilities	<u>(3,313,652)</u>	<u>(3,306,988)</u>
Company	2013 £'000	2012 £'000
Loans and payables at amortised cost	<u>(210,174)</u>	<u>(213,073)</u>
Total financial liabilities	<u>(210,174)</u>	<u>(213,073)</u>
Income tax liabilities	<u>(447)</u>	<u>(99)</u>
Total non-financial liabilities	<u>(447)</u>	<u>(99)</u>
Total liabilities	<u>(210,621)</u>	<u>(213,172)</u>

Deferred Revenue

	2013 £'000	2012 £'000
At 1 January	1,193,602	1,139,261
Additions	77,897	91,876
Amortisation	<u>(41,462)</u>	<u>(37,535)</u>
At 31 December	<u>1,230,037</u>	<u>1,193,602</u>

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

23. TRADE AND OTHER PAYABLES - continued

Derivative Financial Instruments

Exposure to liquidity, credit and market price risk arises as a result of the day to day business activities of the Group and the financing of those activities. Derivative financial instruments are used to hedge exposures to fluctuations in interest rates, foreign exchange rates and commodity prices.

a) Funding and Liquidity Risk

The Group operates a prudent approach to liquidity management using a mixture of long term debt and investments together with short term debt, cash and investments to meet its liabilities when due.

b) Market Risk

Market risk is the risk of loss arising from movements in market variables such as interest rates, exchange rates and commodity prices. Risks are mitigated by utilising appropriate risk management products.

(i) Interest rate risk

The Group's policy on interest rate risk is designed to limit the Group's exposure to floating interest rates.

Consistent with this policy, at 31 December 2013 the Group had 96% (2012: 100%) of net debt at fixed rates.

(ii) Foreign exchange risk

The Group is no longer subject to significant risk relating to foreign exchange.

(iii) Commodity Price Risk

The Group is exposed to price risk on CE Gas revenues.

The Company had no derivative financial instruments at 31 December 2013.

The directors believe that the risks identified above are mitigated by the high proportion of debt which is held at fixed rates and by the financial derivatives which are in place in order to hedge against movements in foreign exchange rates, interest rates and commodity prices. Therefore, any movement in these variables would not have a material effect on the results of the Group.

The directors' consideration of liquidity, interest rate and foreign currency risk are described in the Strategic Report.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

24. FINANCIAL LIABILITIES - BORROWINGS

Group	Book Value		Fair Value	
	2013 £'000	2012 £'000	2013 £'000	2012 £'000
The borrowings are repayable as follows:				
On demand or within one year	112,306	49,217	112,306	49,217
After five years	<u>1,499,770</u>	<u>1,503,992</u>	<u>1,710,152</u>	<u>1,812,130</u>
	<u>1,612,076</u>	<u>1,553,209</u>	<u>1,822,458</u>	<u>1,861,347</u>
Analysis of borrowings:				
Short-term loans	61,599	278	61,599	278
Short-term loans from Group companies	2,349	1,848	2,349	1,848
2020 - 8.875%, Northern Electric Finance plc	100,805	100,697	132,556	141,327
2020 - 9.25%, Northern Powergrid (Yorkshire) plc	238,013	241,405	277,066	293,474
2022 - 7.25%, Northern Powergrid Holdings Company	195,190	194,781	242,550	259,994
2028 - 7.25%, Yorkshire Power Finance Limited	196,448	196,823	232,941	255,290
2035 - 5.125%, Northern Electric Finance plc	152,746	152,679	163,000	170,085
2035 - 5.125%, Northern Powergrid (Yorkshire) plc	203,647	203,557	217,352	227,044
EIB Loans*	276,978	276,944	294,070	310,009
2032 4.375%, Northern Powergrid (Yorkshire) plc	150,187	150,083	149,414	154,591
Cumulative preference shares	<u>34,114</u>	<u>34,114</u>	<u>49,561</u>	<u>47,407</u>
	<u>1,612,076</u>	<u>1,553,209</u>	<u>1,822,458</u>	<u>1,861,347</u>

Company	Book Value		Fair Value	
	2013 £'000	2012 £'000	2013 £'000	2012 £'000
The borrowings are repayable as follows:				
On demand or within one year	15,160	18,507	15,160	18,507
After five years	<u>194,546</u>	<u>194,137</u>	<u>241,906</u>	<u>259,350</u>
	<u>209,706</u>	<u>212,644</u>	<u>257,066</u>	<u>277,857</u>
Analysis of borrowings:				
2028 - 7.25%	195,190	194,781	242,550	259,994
Amounts owed to Group undertakings	<u>14,516</u>	<u>17,863</u>	<u>14,516</u>	<u>17,863</u>
	<u>209,706</u>	<u>212,644</u>	<u>257,066</u>	<u>277,857</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

24. FINANCIAL LIABILITIES - BORROWINGS - continued

Of the total financial liabilities, £1,609,727,000 relates to external borrowings and preference shares whose fair value is determined with reference to quoted market prices. The directors' estimates of the fair value of internal borrowings are determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions or dealer quotes for similar instruments. The valuation of liabilities set out above is based on Level 1 inputs.

As at 31 December 2013, 34,473,672 Northern Electric plc preference shares were held by non-Group undertakings (2012: 34,473,672).

The terms of the cumulative preference shares:

- i) entitle holders, in priority to holders of all other classes of shares, to a fixed cumulative preferential dividend of 8.061p (net) per share per annum payable half-yearly in equal amounts on 31 March and 30 September;
- ii) on a return of capital on a winding up, or otherwise, will carry the right to repayment of capital together with a premium of 99p per share and a sum equal to any arrears or accruals of dividend; this right is in priority to the rights of ordinary shareholders;
- iii) carry the right to attend a general meeting of Northern Electric plc, and vote if, at the date of the notice convening the meeting, payment of the dividend to which they are entitled is six months or more in arrears, or if a resolution is to be considered at the meeting for the winding-up of Northern Electric plc or abrogating, varying or modifying any of the special rights attaching to them; and
- iv) are redeemable in the event of the revocation by the Secretary of State of Northern Electric plc's Public Electricity Supply Licence at the value given in (ii) above.

During the year ended 31 December 2001, under the terms of Northern Electric plc's transfer scheme, as approved by the Secretary of State in accordance with the provisions of the Utilities Act 2000, the Northern Electric plc's Public Electricity Supply Licence was converted into an Electricity Distribution Licence and an Electricity Supply Licence.

At 31 December 2013, the Group had available £130.5m (2012: £162.0m) of undrawn committed borrowing facilities in respect of which all conditions precedent had been met.

The covenants associated with some of the Group's bonds 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 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 any fair value and accounting adjustments.

As at 31 December 2013, the Group's Senior Total Net Debt, as defined by the covenants, totalled £1,511.9m (2012: £1,401.4m).

Using the RAV value as at March 2014 as outlined by Ofgem in its Final Proposals for Distribution Prices published in December 2009 and up rating for the effects of movements in the value of the Retail Prices Index ("RPI") gives an approximation for the RAV value as at December 2013 of £2,703.5m (2012: £2,545.9m). The Senior Total Net Debt to RAV ratio for the Group is therefore estimated at 56% (2012: 55%).

All other loans provided to the Group are unsecured.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

25. PROVISIONS

	Group	
	2013	2012
	£'000	£'000
Provisions	<u>7,555</u>	<u>7,959</u>
Analysed as follows:		
Current	2,851	3,021
Non-current	<u>4,704</u>	<u>4,938</u>
	<u>7,555</u>	<u>7,959</u>

	Abandonment	Claims	Onerous contracts	Other	Total
	£'000	£'000	£'000	£'000	£'000
At 1 January 2013	2,020	2,008	59	3,872	7,959
Utilised/paid in the year	(205)	(1,595)	(31)	(1,338)	(3,169)
Charged to the income statement	-	1,422	-	1,223	2,645
Unwinding of discount	<u>120</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>120</u>
At 31 December 2013	<u>1,935</u>	<u>1,835</u>	<u>28</u>	<u>3,757</u>	<u>7,555</u>

Abandonment: A provision and corresponding asset have been created for the costs of site restoration.

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

Onerous contacts: Related to former retail business property leases. Settlement is expected substantially within the next 12 months.

Other: Relates primarily environmental liabilities, wayleave disputes, provision for future safe disposal of transformers which contain oil contaminated with Polychlorinated Biphenyls (PCBs) and holidays in suspense. Settlement is expected substantially after the next 12 months.

Also included in 'Other' is a provision to cover the actuarial assessment of the costs of unfunded pension arrangements in respect of former employees. Further details can be found in the Employee Benefits Obligation note.

At 31 December 2013, the Company had no provisions for liabilities and charges (2012: £nil).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

26. DEFERRED TAX

	Accelerated tax depreciation £'000	Rollover/ holdover relief £'000	Retirement benefit (obligations) / assets £'000	Other £'000	Total £'000
Group; At 1 January 2013	291,471	16,091	(8,793)	(9,786)	288,983
(Credit)/charge to statement of profit or loss	(37,755)	(2,061)	(5,989)	1,281	(44,524)
Charge to other comprehensive income	-	-	12,320	-	12,320
At 31 December 2013	<u>253,716</u>	<u>14,030</u>	<u>(2,462)</u>	<u>(8,505)</u>	<u>256,779</u>

	Accelerated tax depreciation £'000	Rollover/ holdover relief £'000	Retirement benefit (obligations)/ assets £'000	Other £'000	Total £'000
Group; At 1 January 2012 (as previously reported)	332,173	17,393	50,056	(10,691)	388,931
Prior year adjustment	-	-	(53,850)	-	(53,850)
At 1 January 2012 (as restated)	332,173	17,393	(3,794)	(10,691)	335,081
(Credit)/charge to statement of profit or loss (as previously reported)	(41,001)	(1,302)	5,781	905	(35,617)
(Credit)/Charge to statement of profit or loss (prior year adjustment)	299	-	(9,890)	-	(9,591)
Credit to other comprehensive income (prior year adjustment)	-	-	(890)	-	(890)
At 31 December 2012 (as restated)	<u>291,471</u>	<u>16,091</u>	<u>(8,793)</u>	<u>(9,786)</u>	<u>288,983</u>

The other deferred tax asset primarily represents the tax benefit on interest accrued on loans from parent undertakings, fair value adjustments on borrowings acquired on the acquisition of Yorkshire Power Group Limited and cash flow hedges.

Movement in the year represents deferred tax on the movement in retirement benefit obligation/asset. A proportion of the movement has been capitalised in property, plant and equipment.

The Company had no deferred tax liability as at 31 December 2013 (2012: £nil).

27. EMPLOYEE BENEFIT OBLIGATIONS

Introduction

Northern Electric plc operates two pension schemes on behalf of the participating companies within the Group:

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

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

27. EMPLOYEE BENEFIT OBLIGATIONS - continued

Introduction - continued

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

The Group does not provide any other post-retirement benefits to members of the DB Scheme.

Role of Trustees

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

Funding requirements

UK legislation requires that pension schemes are funded prudently (i.e. to a level in excess of the current expected cost of providing benefits). The last actuarial valuation of the DB scheme was carried out by the Group Trustees' actuarial advisors, Aon Hewitt, as at 31 March 2010. Such valuations are required by law to take place at intervals of no more than three years and, therefore, an actuarial valuation is currently ongoing with an effective date of 31 March 2013. Following each valuation, the Trustees and Northern Electric plc must agree the contributions required (if any) to ensure the DB Scheme is fully funded over time on the basis of suitable, prudent assumptions. Contributions agreed in this manner constitute a minimum funding requirement.

Agreement was reached during June 2011 with the Group Trustees to repair the funding deficit of £276m as at 31 March 2010 over the 15 year period to 31 March 2025, subject to the actuarial assumptions adopted for the triennial valuation as at 31 March 2010 being borne out in practice. The agreement includes cash payments of £29.9m per annum over the period to 31 March 2015, made on a monthly basis, followed by an agreed profile of payments to be made over the remaining ten years of the recovery plan, as set out below:

1 April 2015 to 31 March 2016	£24.5m p.a.
1 April 2016 to 31 March 2023	£16.3m p.a.
1 April 2023 to 31 March 2025	£17.4m p.a.

All contributions set out above are in 2010/11 prices and increase in line with increases in RPI over the period until they fall due. However, this recovery plan is currently under review as part of the actuarial valuation as at 31 March 2013.

The contributions payable by the Group to the DB Scheme in respect of future benefits, which are accruing, are 47.0% (for certain senior management) and 29.4% (for other employees) of pensionable pay. These contributions were determined as part of the 31 March 2010 actuarial valuation and are payable in addition to the deficit repair contributions mentioned above. These rates will remain in place until such a time as a new schedule of contributions is agreed between the Trustees and Northern Electric plc as part of the 31 March 2013 valuation.

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

27. EMPLOYEE BENEFIT OBLIGATIONS - continued

Pensions' Regulation

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

- protect the benefits of members;
- promote and to improve understanding of the good administration; and
- reduce the risk of situations arising which may lead to compensation being payable from the Pension Protection Fund (PPF).

The Pensions Regulator has various powers including the power to:

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

Reporting at 31 December 2013

For the purposes of this disclosure, the current and future pension costs of the Group have been assessed by Aon Hewitt, a qualified independent actuary, using the assumptions set out below, which the actuary has confirmed represent a reasonable best estimate of those costs. This review has been based on the same membership and other data as at 31 March 2010. The board has accepted the advice of the actuary and formally approved the use of these assumptions for the purpose of calculating the pension cost of the Group.

The results of the latest funding valuation at 31 March 2010 have been adjusted to 31 December 2013. Those adjustments take account of experience over the period since 31 March 2010, changes in market conditions, and differences in the financial and demographic assumptions. The present value of the Defined Benefit Obligation (the "DBO") and the related current service cost were measured using the Projected Unit Credit Method.

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

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

Main financial assumptions	2013 % p.a.	2012 % p.a.
RPI Inflation	3.15	2.80
Rate of general long-term increase in salaries	3.15	2.80
Pension increases	3.05	2.80
Discount rate for scheme liabilities	4.40	4.40

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

Main financial assumptions	2013	2012
Life expectancy for a male currently aged 60	27.1	27.9
Life expectancy for a female currently aged 60	28.8	28.1
Life expectancy at 60 for a male currently aged 45	28.8	29.6
Life expectancy at 60 for female currently aged 45	30.6	29.8
Proportion of pension exchanged for additional cash at retirement	10%	0%

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

27. EMPLOYEE BENEFIT OBLIGATIONS - continued

Reporting at 31 December 2013 - continued

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

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

Main financial assumptions	2013 £m	2012 £m
Developed market equity	290.7	288.1
Emerging market equity	12.1	15.7
Property	112.2	103.4
Reinsurance	61.8	59.4
Listed infrastructure	66.8	0.0
Investment grade corporate bonds	331.2	330.7
Other debt	37.2	33.3
Fixed interest gilts	21.6	16.4
Index-linked gilts	358.7	357.9
Cash	18.4	17.9
Total	<u>1,310.7</u>	<u>1,222.8</u>

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

As at 31 December 2013, the fair value of the DB Scheme's assets, which related to self-investment, amounted to £nil (2012: £nil).

The amounts recognised on the statement of financial position are set out below:

Reconciliation of funded status to statement of financial position	2013 £m	2012 as restated £m
Fair value of DB Scheme assets	1,310.7	1,222.8
Present value of funded defined benefit obligations	<u>(1,321.3)</u>	<u>(1,259.3)</u>
Funded status	(10.6)	(36.5)
Present value of unfunded defined benefit obligations	<u>(1.7)</u>	<u>(1.7)</u>
Liability recognised on the statement of financial position	<u>(12.3)</u>	<u>(38.2)</u>

The amounts recognised in comprehensive income or in property, plant and equipment are set out below.

	2013 £m	2012 as restated £m
Operating cost		
Service costs:		
Current service cost	13.9	12.2
Administration expenses	1.5	1.0
Financing cost		
Interest on net defined benefit liability	<u>0.8</u>	<u>(0.2)</u>
Pension expense	<u>16.2</u>	<u>13.0</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

27. EMPLOYEE BENEFIT OBLIGATIONS - continued

Re-measurements in OCI:	2013	2012 as restated
	£m	£m
Return on plan assets in excess of that recognised in net interest	(36.4)	(40.3)
Actuarial losses due to changes in financial assumptions	57.6	83.3
Actuarial gains due to changes in demographic assumptions	(23.2)	-
Actuarial losses due to liability experience	10.7	17.0
Total amount recognised in OCI	8.7	60.0
Total	24.9	73.0
	2013	2012 as restated
	£m	£m
Pension expense	16.2	13.0
Allocated to the statement of profit or loss	7.4	7.2
Allocated to property, plant and equipment	8.8	5.8
Changes to the present value of the defined benefit obligation during the year	2013	2012 as restated
	£m	£m
Opening defined benefit obligation	1,259.3	1,141.8
Current service cost	13.9	12.2
Interest expense on DBO	54.6	53.9
Contributions by DB Scheme participants	1.6	1.8
Actuarial gains on DB Scheme liabilities arising from changes in demographic assumptions	(23.2)	-
Actuarial losses on DB Scheme liabilities arising from changes in financial assumptions	57.6	83.3
Actuarial losses on DB Scheme liabilities arising from experience	10.7	17.0
Net benefits paid out	(53.2)	(50.7)
Closing defined benefit obligation	1,321.3	1,259.3
Changes to the fair value of DB Scheme assets during the year	2013	2012 as restated
	£m	£m
Opening fair value of DB Scheme assets	1,222.8	1,128.2
Interest income on DB Scheme assets	53.8	54.1
Re-measurement gains on DB Scheme assets	36.4	40.3
Contributions by the employer	50.8	50.1
Contributions by DB Scheme participants	1.6	1.8
Net benefits paid out	(53.2)	(50.7)
Administration costs incurred	(1.5)	(1.0)
Closing fair value of scheme assets	1,310.7	1,222.8

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

27. EMPLOYEE BENEFIT OBLIGATIONS - continued

	2013	2012 as restated
Actual return on DB Scheme assets	£m	£m
Interest income on DB Scheme assets	53.8	54.1
Re-measurement gains on DB Scheme assets	36.4	40.3
Closing fair value of scheme assets	90.2	94.4
Analysis of amounts recognised in OCI	£m	£m
Total re-measurement losses	(8.7)	(60.0)
Total loss	(8.7)	(60.0)

Profile of the DB Scheme

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

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

Risks associated with the DB Scheme

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

Risk	Description	Mitigation
Volatile asset returns	The DBO is calculated using a discount rate set with reference to corporate bond yields. If assets underperform this discount rate, this will create an element of deficit. The DB Scheme holds a significant proportion (29%) of its assets in growth assets (such as equities) which, although expected to outperform corporate bonds in the long-term, create volatility and risk in the short-term.	To avoid concentration risk, the allocation to UK equity is restricted to approximately 35% of the total equity allocation. The allocation to growth assets is monitored to ensure it remains appropriate given the DB Scheme's long-term objectives. The Trustees regularly review the strategy in respect of growth seeking assets and have recently diversified some return-seeking assets from equities into Reinsurance and Listed Infrastructure to reduce overall risk.
Changes in bond yields	A decrease in corporate bond yields will increase the value placed on the DBO for accounting purposes, although this will be partially offset by an increase in the value of the DB Scheme's bond holdings.	The DB Scheme also holds a substantial proportion of its assets (35%) as bonds, which provide a hedge against movements in the DBO. There are some differences in the credit quality of bonds held by the DB Scheme and the bonds analysed to decide the DBO discount rate, such that there remains some risk should yields on different quality bond/swap assets diverge.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

27. EMPLOYEE BENEFIT OBLIGATIONS - continued

Risks associated with the DB Scheme – continued

Inflation risk	A significant proportion of the DBO is indexed in line with price inflation (specifically in line with RPI) and higher inflation will lead to higher liabilities	The DB Scheme holds around 30% in UK government index-linked bonds which provide a hedge against higher than expected inflation increases of the DBO (rising inflation will increase both the DBO and the value of the index-linked bond portfolio).
Currency risk	To increase diversification, the DB Scheme invests in overseas assets. This leads to a risk that foreign currency movements negatively impact the value of assets in Sterling terms.	The DB Scheme hedges a proportion of the overseas investments currency risk for those overseas currencies that can be hedged efficiently. The DB Scheme's currency hedging ratio is currently 50% in respect of overseas developed market currencies.
Life expectancy	The majority of the DB Scheme's obligations are to provide benefits for the pensionable lifetime of the member, so increases in life expectancy will result in an increase in the liabilities.	The DB Scheme regularly reviews actual experience of its membership against the actuarial assumptions underlying the future benefit projections and carries out detailed analysis when setting an appropriate scheme specific mortality assumption.

Other risks

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

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

Sensitivity to key assumptions

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

	Changes in DBO	Revised DBO
Current Figures	1,321.3	
Following a 10 bps decrease in the discount rate	22.7	1,344.0
Following a 10 bps increase in the discount rate	(22.3)	1,299.0
Following a 10 bps increase in the inflation assumption	14.4	1,335.7
Following a 10 bps decrease in the inflation assumption	(21.3)	1,300.0
Following a 1 year increase in life expectancy	40.4	1,361.7
Following a 1 year decrease in life expectancy	(41.0)	1,280.3

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

27. EMPLOYEE BENEFIT OBLIGATIONS - continued

Sensitivity to key assumptions - continued

A provision to cover the actuarial assessment of the costs of unfunded pension arrangements in respect of former employees has been made by the Group and Company as follows:

	£m
At 1 January 2013	1.7
Utilised/paid in the year	(0.1)
Transferred from statement of profit or loss	0.1
	<u>1.7</u>
At 31 December 2013	<u>1.7</u>

28. RELATED PARTY DISCLOSURES

GROUP

Details of transactions between the Group and other related parties are disclosed below.

Trading transactions

During the year, Group entities entered into the following transactions with related parties that are not members of the Group:

Related Party	Sales to related parties £'000	Purchases from related parties £'000	Amounts owed to related parties £'000
2013:			
CE Insurance Services Limited	-	1,189	-
Vehicle Lease and Service Limited	<u>169</u>	<u>8,064</u>	<u>1,082</u>
2012			
CE Insurance Services Limited	-	1,322	-
Vehicle Lease and Service Limited	<u>163</u>	<u>7,760</u>	<u>1,028</u>

Loans

The Group has received loans from companies in the MidAmerican Energy Holdings Company group. The total interest included in finance costs in the statement of profit or loss for the year ended 31 December 2013 was £nil (2012: £83,000). Included within borrowing is £2,349,000 as at 31 December 2013 (2012: £1,848,000).

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

COMPANY

Details of transactions between the Company and other related parties are disclosed below.

Loans

The Company has advanced loans to other companies in the Group. The total interest included in investment income in the statement of profit or loss for the year ended 31 December 2013 was £18,491,000 (2012: £18,491,000). Included within loans and other financial assets is £264,158,000 as at 31 December 2013 (2012: £264,158,000).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued
FOR THE YEAR ENDED 31 DECEMBER 2013

28. RELATED PARTY DISCLOSURES - continued

Loans - continued

The Company has received loans from other companies in the Group. The total interest included in finance costs in the statement of profit or loss for the year ended 31 December 2013 was £267,000 (2012: £14,840,000). Included within borrowings is £14,948,000 as at 31 December 2013 (2012: £17,948,000).

29. RECONCILIATION OF PROFIT BEFORE INCOME TAX TO CASH GENERATED FROM OPERATIONS

Group

	2013	2012 as restated
	£'000	£'000
Profit before income tax	280,554	283,152
Depreciation charges	159,143	146,598
Profit on disposal of fixed assets	(759)	(637)
Amortisation of deferred revenue	(41,462)	(37,535)
Retirement benefit obligations	(34,600)	(30,698)
(Decrease)/increase in provisions	(404)	234
Finance costs	87,519	88,237
Finance income	(933)	(616)
	449,058	448,735
Decrease in inventories	361	2,945
Decrease/(increase) in trade and other receivables	23,333	(19,932)
Decrease in trade and other payables	(24,688)	(9,696)
Cash generated from operations	448,064	422,052

Company

	2013	2012
	£'000	£'000
Profit before income tax	3,292	3,284
Finance costs	15,176	15,218
Finance income	(18,491)	(18,491)
	(23)	11
Increase in trade and other payables	39	37
Cash generated from operations	16	48

30. ULTIMATE CONTROLLING PARTY

The ultimate controlling party and ultimate parent undertaking of Northern Powergrid Holdings Company is Berkshire Hathaway, Inc., a company incorporated in the United States of America.

Copies of the group accounts of Berkshire Hathaway, Inc., which include Northern Powergrid Holdings Company, can be obtained from the Company Secretary, Northern Powergrid Holdings Company, Lloyds Court, 78 Grey Street, Newcastle upon Tyne, NE1 6AF.