



EASTERN POWER NETWORKS PLC

Registered Number 2366906

ANNUAL REPORT AND FINANCIAL STATEMENTS

31 December 2012

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Directors

Andrew John Hunter
Neil Douglas McGee
Hok Shan Chong
Hing Lam Kam
Basil Scarsella
Charles Chao Chung Tsai
Sui See Yuen
Mei Fan Ngan
Duncan Nicholas Macrae
Loi Shun Chan
Kee Ham Chan
Chi Tin Wan

Company Secretary

Christopher Baker

Auditor

Deloitte LLP
2 New Street Square
London
EC4A 3BZ

Registered Office

Newington House,
237 Southwark Bridge Road
London
SE1 6NP

DIRECTORS' REPORT

The Directors present their annual report and financial statements for the year ended 31 December 2012

Principal activity and review of the business

The Company's principal activity during the year continued to be the distribution of electricity to domestic, commercial and industrial customers through network ownership, management, operation, maintenance and renewal. It will continue in this activity for the foreseeable future.

Business Review

The profit for the year, before taxation, amounted to £183.9m (2011: £75.6m) and after taxation to £189.6m (2011: £86.0m). Dividends of £55.0m were paid in the year (2011: £75.0m).

Significant investment in the electricity networks continued in the year. The capital expenditure programme was focused on network replacement, reinforcement, expansion and driving improved network performance.

The Company measures the achievement of its objectives through the use of quantitative assessments and (where quantitative means are less relevant) through the use of qualitative assessments. The principal key performance indicators ('KPIs') are set out below.

	2012	2011	Change
	£m	£m	%
Financial key performance indicators			
Turnover	522.2	464.7	12%
Earnings before interest, tax, depreciation and amortisation (EBITDA) ¹	334.3	279.0	20%
Capital expenditure net of customer contributions	244.0	251.3	-3%
Net debt ²	1,488.2	1,383.8	8%
Regulatory asset value (RAV) ³	2,180.0	2,062.7	5%
Ratio of net debt to RAV	68%	67%	
Non financial key performance indicators			
Customer Minutes Lost per customer (CML)	48.0	49.7	-3%
Customer Interruptions per 100 customers (CI)	56.0	64.1	-13%

¹ EBITDA is a non-statutory measure, and is calculated by adding back amortisation and depreciation to operating profit.

² Net debt is defined as borrowings (excluding derivatives) net of cash and cash equivalents.

³ "RAV" is defined as Ofgem Regulatory Asset Value plus allowable additions less regulatory depreciation.

The UK Power Networks group ("the Group") manages its operations on a business segment basis. For this reason, the Company's Directors believe that further key performance indicators for the Company are not necessary or appropriate for an understanding of the development, performance or position of the business.

Future developments

The Directors aim to deliver the right balance of customer service and shareholder return through efficient investment in the Network within the boundaries of the price control allowances set by the Regulator, the Office of Gas and Electricity Markets ("Ofgem"). The current price control allowances were set under the fifth electricity distribution price control review ("DPCR5") and are effective from 1 April 2011 to 31 March 2015. The Directors believe the Company will continue to operate as a profitable, sustainable business under the DPCR5 price control allowances.

DIRECTORS' REPORT continued

Directors

Directors who held office during the year and subsequently were as follows

Andrew John Hunter	
Neil Douglas McGee	
Hok Shan Chong	
Edmond Tak Chuen Ip	(resigned on 15 October 2012)
Hing Lam Kam	
Basil Scarsella	
Charles Chao Chung Tsai (Alternate director)	
Kai Sum Tso	(resigned on 8 February 2013)
Sui See Yuen	
Mei Fan Ngan (Alternate director)	
Duncan Nicholas Macrae	
Loi Shun Chan	(appointed on 10 September 2012)
Kee Ham Chan (Alternate director)	(appointed on 10 September 2012)
Chi Tin Wan	(appointed on 8 February 2013)

None of the Directors had a service contract with the Company in the current or prior year

The Company has made qualifying third party indemnity provisions for the benefit of its directors which were made during the year and remain in force at the date of this report

Financial risk management

The Group develops and implements risk management policies and procedures and promotes a robust control environment at all levels of the organisation. Further details of the principal risks and risk management activities are included within the UK Power Networks Holdings Limited accounts

The Company is exposed to financial risk through its financial assets and liabilities. The key financial risk is that the proceeds from financial assets are not sufficient to fund the obligations arising from liabilities as they fall due. The most important components of financial risk are interest rate risk, currency risk, credit risk, liquidity risk, cash flow risk and price risk. Due to the nature of the Company's business and the assets and liabilities contained within the Company's balance sheet the only financial risks the Directors consider relevant to this Company are credit risk, liquidity risk, interest rate risk and price risk.

Credit and liquidity risk

The Company finances its operation by a mixture of cash generated from operations, bank borrowings, Group loans, long-term loans and commercial paper. The Company has borrowings denominated in sterling at fixed rates of interest.

Liquidity risk is managed by spreading debt maturities over a wide range of dates thereby ensuring that the Company is not subject to excessive financing risk in any one year. Derivative instruments are used to manage the risks identified.

The credit risk on liquid funds and financial instruments is limited because the counterparties are reputable banks and building societies. The Company is required by the distribution licence to maintain an investment grade rating and has secured a rating of BBB+ (or the equivalent) from Standard and Poor's, Moodys and Fitch. The Company is able to raise finance in external financial markets supported by cash flows generated by the Regulatory Asset Value which determines the levels of allowed revenue that may be recovered.

DIRECTORS' REPORT continued

Interest rate risk

The Company's exposure to interest rate fluctuations on its borrowings is managed by maintaining an appropriate mix of fixed, index linked and floating rate debt. Interest rate swaps are used to convert a portion of fixed rate debt to floating rate in the long term but maintain a fixed rate for the duration of the five year regulatory price control period. When appropriate, swap instruments are employed to lock in UK Gilt rates in anticipation of future financing to reduce exposure to the variability of future interest cash flows. In addition index linked swaps are used to create Retail Price Index ("RPI") exposure within interest costs which naturally offsets the RPI exposure of the Company's regulated income.

The use of financial derivatives is governed by the Group's policies approved by the Board of Directors, which provide written principles on the use of financial derivatives to manage these risks. The Group does not use derivative financial instruments for speculative purposes.

Price risk

The prices the Company is allowed to charge for its services are for the most part subject to regulatory controls. The profitability of the Company's operations is thus largely dependent upon the successful management of costs incurred to deliver the services and maintain and expand the network in compliance with its operating licence. The Directors believe that the Company is in a position to operate profitably within these constraints.

Financial instruments

The Company holds or issues financial instruments for two main purposes:

- to finance its operations, and
- to manage the interest rate risks arising from its sources of finance.

The Company finances its operation by a mixture of retained profits, long-term loans and commercial paper. The Company has borrowings denominated in sterling at fixed rates of interest. The main risk arising from the Company's financial instruments is interest rate risk. The Company's policy for managing this risk is as above and is defined in statements authorised by the Board of Directors and reviewed on an annual basis. Authority for managing risk consistent with this corporate policy may be delegated by the Board to, amongst others, the Treasury department of the parent company, UK Power Networks Holdings Limited.

Going concern

The Company operates the regulated electricity distribution networks in the East Anglia / North London area. The revenue of the Company is regulated by Ofgem via established price control mechanisms. The Company has considerable financial resources together with committed facilities.

As at 31 December 2012 the Company had borrowings (excluding derivatives) of £1,505.9m (2011: £1,440.7m) of which £17.0m (2011: £250.0m) was short term. The Company has access to a £210.0m (2011: £212.0m) revolving credit facility of which £120.0m (2011: £nil) was drawn at the balance sheet date. The business has the ability to access external debt markets supported by cash generated by operations as a result of financial returns earned against the regulatory asset base. The Company trades with high quality customers with strong financial standing and together with the regulatory contract this means that the Company's cash flows are reasonably assured.

The Company's forecasts and projections, taking into account reasonable possible changes in trading performance, show that the Company should be able to operate within the level of its current facilities. As a result the Directors are satisfied that the Company has adequate resources to continue operating for the foreseeable future and therefore continue to adopt the going concern basis in preparing its financial statements. This conclusion is based on the availability of facilities set out above, the relatively stable and regulated nature of the business, the forecast long-term plan and the anticipated ability of the Group to be able to raise additional long-term debt in the future.

DIRECTORS' REPORT continued

Creditors payment policy

The Company's current policy concerning the payment of its trade creditors and other suppliers is to

- agree the terms of payment with those creditors/suppliers when agreeing the terms of each transaction,
- ensure that those creditors/suppliers are made aware of the terms of payment by inclusion of the relevant terms in contracts, and
- pay in accordance with its contractual and other legal obligations

The payment policy applies to all payments to creditors/suppliers for revenue and capital supplies of goods and services without exception. At 31 December 2012, the Company had an average of 6 days (2011 nil days) purchases outstanding in its trade creditors

Political and charitable contributions

The Company made no charitable or political contributions in either year

Disclosure of information to Auditor

Each of the persons who is a director at the date of approval of this annual report confirms that

- so far as the Director is aware, there is no relevant audit information of which the Company's Auditor is unaware, and
- the Director has taken all the steps that they ought to have taken as a director in order to make themselves aware of any relevant audit information and to establish that the Company's 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 have expressed their willingness to continue in office as Auditor and a resolution to reappoint them will be proposed at the forthcoming Annual General Meeting

Approved by the Board and signed on its behalf by



B Scarsella
Director
19 March 2013

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The Directors are responsible for preparing the Annual Report 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 United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). 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 the affairs of the Company and of the profit and loss of the Company for the year. In preparing these financial statements, the Directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgements and estimates that are reasonable and prudent,
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements, and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company 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 hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

The Directors confirm to the best of their knowledge that

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets and liabilities, financial position and profit of Eastern Power Networks plc as at 31 December 2012, and
- the Directors' report includes a true and fair view of the development and performance of the business and the financial position of Eastern Power Networks plc together with a description of its principal risks and uncertainties.

Signed on behalf of the Board of Directors of Eastern Power Networks plc on 19 March 2013



B Scarsella
Director

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF EASTERN POWER NETWORKS PLC

We have audited the financial statements of Eastern Power Networks plc for the year ended 31 December 2012 which comprise the Profit and Loss Account, the Balance Sheet, the Statement of Total Recognised Gains and Losses and the related notes 1 to 22. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

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 an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and Auditor

As explained more fully in the Directors' Responsibilities Statement, 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 Company's circumstances 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 annual report to identify material inconsistencies with the audited financial statements. 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 affairs as at 31 December 2012 and of its profit for the year then ended,
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report 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, or returns adequate for our audit have not been received from branches not visited by us, or
- the financial statements 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.



James Leigh FCA (Senior statutory auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditors
London, United Kingdom
19 March 2013

**PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDED 31 DECEMBER 2012**

	Note	2012 £m	2011 £m
Turnover	2	522 2	464 7
Cost of sales		(22 9)	(18 5)
Gross profit		499 3	446 2
Distribution costs		(232.8)	(230 8)
Administrative expenses		(2 9)	(2 9)
Operating profit	3	263 6	212 5
Finance charges (net)			
Interest receivable and similar income	5	5.8	4 8
Interest payable and similar charges	5	(66.2)	(53 4)
Fair value losses on financial instruments	5	(19 3)	(88 3)
		(79 7)	(136 9)
Profit on ordinary activities before taxation		183 9	75 6
Tax on profit on ordinary activities	6	5 7	10 4
Profit for the financial year	17	189 6	86 0

All results are derived from continuing operations in both the current and preceding year

**STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES
FOR THE YEAR ENDED 31 DECEMBER 2012**

	<i>Note</i>	2012 £m	2011 £m
Profit for the financial year		189.6	86.0
Actuarial gain/(loss) on defined pension benefits	19	0.1	(32.6)
Deferred tax attributable to actuarial loss	19	-	8.2
Deferred tax rate change relating to historical actuarial losses	19	(1.7)	(1.4)
Losses on cash flow hedges	17	-	(18.3)
Deferred tax attributable to losses on cash flow hedges	17	-	4.6
Transfer to profit or loss on cashflow hedges	17	3.2	0.8
Deferred tax attributable to transfer to profit or loss	17	(0.7)	(0.2)
Deferred tax rate change attributable to cash flow hedges	17	(0.3)	-
Total recognised gains and losses relating to the year		190.2	47.1

The deferred tax rate change refers to the reduction in main stream corporation tax from 25% to 23% from 1 April 2013 (2011: 27% to 25% from 1 April 2012)

**BALANCE SHEET
AT 31 DECEMBER 2012**

	Note	2012 £m	2011 £m
Fixed assets			
Tangible assets	7	2,755.7	2,583.1
Current assets			
Debtors			
- amounts falling due within one year	8	90.5	67.6
- amounts falling due after more than one year	8	203.6	210.0
Investments - unlisted money market investments		-	45.0
Cash at bank and in hand		17.7	11.9
		311.8	334.5
Creditors, amounts falling due within one year	9	(225.1)	(477.5)
Net current assets/(liabilities)		86.7	(143.0)
Total assets less current liabilities		2,842.4	2,440.1
Creditors, amounts falling due after more than one year	10	(1,586.3)	(1,305.7)
Provision for liabilities	14	(252.8)	(265.4)
Net assets excluding pension liability		1,003.3	869.0
Pension liability	19	(59.7)	(60.6)
Net assets including pension liability		943.6	808.4
Capital and reserves			
Called up share capital	15	125.8	125.8
Share premium account	17	5.6	5.6
Capital redemption reserve	17	10.6	10.6
Hedging reserve	17	(10.9)	(13.1)
Profit and loss account	17	812.5	679.5
Shareholder's funds		943.6	808.4

The financial statements of Eastern Power Networks plc, registered number 2366906, were approved by the Board of Directors and authorised for issue on 19 March 2013
They were signed on its behalf by



B Scarsella
Director

NOTES TO THE FINANCIAL STATEMENTS

1. Accounting policies

The principal accounting policies are set out below. They have all been applied consistently throughout the year and the preceding year, except as detailed below.

Basis of preparation

These financial statements have been prepared under the historical cost convention and in accordance with applicable United Kingdom law and accounting standards, except that certain derivative financial instruments are recorded at fair value and except as noted below in respect of tangible fixed assets.

The Company is exempt from preparing a cash flow statement under the terms of FRS 1 'Cash flow statements (revised 1996)' as it is a member of a group, headed by UK Power Networks Holdings Limited whose consolidated accounts include a cash flow statement and are publicly available.

The Company is exempt from the disclosures required by FRS 29 'Financial Instruments: Disclosures' since the Company is a subsidiary of UK Power Networks Holdings Limited which prepares consolidated accounts under UK GAAP that comply with the requirements of FRS 29.

FRS 25 "Financial instruments: disclosure and presentation" and FRS 26 "Financial instruments: recognition and measurement" have been applied in the recognition of interest swaps novated to the Company on 26 January 2011. The application of FRS 25 and FRS 26 affects the Company balance sheet principally in respect of derivative financial instruments which are recognised in the balance sheet at their fair value as financial assets or liabilities. The carrying values of borrowings held by the Company which are designated within an effective fair value hedge relationship are also adjusted to reflect movements associated with the hedged risks. The accounting policy is described more fully in the derivative financial instruments policy below.

Going concern

The financial statements have been prepared on the going concern basis. The grounds for adopting this basis are discussed in the Directors' report on page 4.

Tangible fixed assets

Tangible fixed assets are stated at cost, net of depreciation and provision for impairment. The carrying values of tangible fixed assets are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable.

Depreciation is provided on all tangible fixed assets other than freehold land, at rates calculated to write off the cost, less estimated residual value based on prices prevailing at the date of acquisition, of each asset evenly over its expected useful life, as follows:

Overhead and underground lines	–	45 to 60 years
Other network plant and buildings	–	20 to 60 years
Fixtures and equipment	–	5 years
Vehicles	–	5 to 10 years

Assets in the course of construction are carried at cost, less any recognised impairment loss. Depreciation of these assets, on the same basis as other assets, commences when the assets are ready for their intended use.

NOTES TO THE FINANCIAL STATEMENTS continued

1. Accounting policies continued

Tangible fixed assets continued

Customer contributions in respect of capital expenditure are credited to a fixed asset account and are released to the profit and loss account over the expected useful lives of the relevant assets by equal annual instalments. The unamortised amount of such contributions is shown as a deduction from fixed assets. This is a departure from the Companies Act 2006, which requires fixed assets to be included at their purchase price or production cost and hence the contribution would be presented as deferred income. However, contributions relate directly to the cost of fixed assets used in the distribution network and it is the opinion of the Directors that the treatment adopted is necessary to give a true and fair view. The value of the contributions is shown in Note 7.

Finance costs

Finance costs of debt are recognised in the profit and loss account over the term of such instruments, at a constant rate on the carrying amount.

Finance costs which are directly attributable to the construction of tangible fixed assets are capitalised as part of the cost of these assets. The commencement of capitalisation begins when both finance costs and expenditure for the assets are being incurred and activities that are necessary to get the asset ready for use are in progress. Capitalisation ceases when substantially all the activities that are necessary to get the asset ready for use are complete.

Taxation

Current tax, including UK corporation tax, is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more or a right to pay less tax in the future have occurred at the balance sheet date, with the following exceptions:

- provision is made for gains on disposal of fixed assets that have been rolled over into replacement assets only where, at the balance sheet date, there is a commitment to dispose of the replacement assets with no likely subsequent rollover or available capital losses,
- provision is made for gains on re-valued fixed assets only where there is a commitment to dispose of the re-valued assets and the attributable gain can neither be rolled over nor eliminated by capital losses, and
- deferred tax assets are recognised only to the extent that the Directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing difference can be deducted.

Deferred tax is measured on an undiscounted basis.

Investments

Current asset investments are stated at the lower of cost and net realisable value.

Financial instruments

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

NOTES TO THE FINANCIAL STATEMENTS continued

1. Accounting policies continued

Financial Instruments continued

Financial assets

Trade debtors

Trade debtors are initially recognised at fair value. The carrying amount is reduced through the use of an allowance account. Appropriate allowances for estimated irrecoverable amounts are recognised where the estimated cash flows are less than the carrying amount. 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 profit or loss.

Cash and cash equivalents

Cash and cash equivalents comprise cash on hand and demand deposits, and other short-term highly liquid investments that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value.

Financial liabilities

Financial liabilities are classified as either financial liabilities 'at fair value through profit or loss (FVTPL)' or 'other financial liabilities'.

Financial liabilities at FVTPL

Financial liabilities are classified as at FVTPL where the financial liability is either held for trading or it is designated as at FVTPL.

A financial liability is classified as held for trading if

- it has been incurred principally for the purpose of disposal in the near future, or
- it is a part of an identified portfolio of financial instruments that the Company manages together and has a recent actual pattern of short-term profit-taking, or
- it is a derivative that is not designated and effective as a hedging instrument.

A financial liability other than a financial liability held for trading may be designated as at FVTPL upon initial recognition if

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise, or
- the financial liability forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Company's documented risk management or investment strategy, and information about the Company is provided internally on that basis, or
- it forms part of a contract containing one or more embedded derivatives, and FRS 26 'Financial Instruments: Recognition and Measurement' permits the entire combined contract (asset or liability) to be designated as at FVTPL.

Financial liabilities at FVTPL are stated at fair value, with any resultant gain or loss recognised in profit or loss. The net gain or loss recognised in profit or loss incorporates any interest paid on the financial liability.

Other financial liabilities

Other financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs. Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis. The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

De-recognition of financial liabilities

The Company derecognises financial liabilities when, and only when, the Company's obligations are discharged, cancelled or they expire.

NOTES TO THE FINANCIAL STATEMENTS continued

1. Accounting policies continued

Derivative financial instruments

The Company uses derivative financial instruments to reduce exposure to interest rate and inflation rate movements. The Company does not hold or issue derivative financial instruments for speculative purposes.

Interest rate and inflation rate swaps are entered into for the purpose of matching or eliminating risk from potential movements in interest and inflation rates associated with the borrowing requirements of the Company. Amounts payable or receivable in respect of the interest and inflation rate swaps are recognised within net interest payable in the profit and loss account over the life of the financial instrument.

Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently remeasured to their fair value at each balance sheet date. The resulting gain or loss is recognised in the profit and loss account immediately unless the derivative is designated and effective as a hedging instrument, in which event the timing of the recognition in the profit and loss account depends on the nature of the hedge relationship. The Company designates certain derivatives as either hedges of the fair value of recognised assets or liabilities or firm commitments (fair value hedges) or hedges of highly probable forecast transactions (cash flow hedges).

A derivative with a positive fair value is recognised as a financial asset whereas a derivative with a negative fair value is recognised as a financial liability. A derivative is presented as a non-current asset or a non-current liability if the remaining maturity of the instrument is more than 12 months and it is not expected to be realised or settled within 12 months. Other derivatives are presented as current assets or current liabilities.

Hedge accounting

At the inception of the hedge relationship, the Company documents the relationship between the hedging instrument and the hedged item, along with its risk management objectives and its strategy for undertaking various hedge transactions. Furthermore, at the inception of the hedge and on an ongoing basis, the Company documents whether the hedging instrument is highly effective in offsetting changes in fair values or cash flows of the hedged item.

The 'Financial instruments' note below sets out details of the fair values of the derivative instruments used for hedging purposes.

Movements in the hedging reserve in equity are detailed in the reserves note below.

Fair value hedges

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the profit and loss account immediately, together with any changes in the fair value of the hedged item that are attributable to the hedged risk. The change in the fair value of the hedging instrument and the change in the hedged item attributable to the hedged risk are recognised in the line of the income statement relating to the hedged item.

Fair value hedge accounting is discontinued when the Company revokes the hedging relationship, the hedging instrument expires or is sold, terminated, or exercised, or no longer qualifies for hedge accounting. The fair value adjustment to the carrying amount of the hedged item arising from the hedged risk is amortised to the profit and loss account from that date.

NOTES TO THE FINANCIAL STATEMENTS continued

1. Accounting policies continued

Hedge accounting continued

Cash flow hedges

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are deferred through the Statement of Total Recognised Gains and Losses. The gain or loss relating to the ineffective portion is recognised immediately in the profit and loss account, and is included in the 'finance charges' line.

Amounts previously recognised in the Statement of Total Recognised Gains and Losses are reclassified to the profit and loss account in the periods when the hedged item is recognised in the profit and loss account, in the same line of the profit and loss account as the recognised hedged item.

Cash flow hedge accounting is discontinued when the Company revokes the hedging relationship, the hedging instrument expires or is sold, terminated, or exercised, or no longer qualifies for hedge accounting. Any gain or loss recognised in the Statement of Total Recognised Gains and Losses at that time remains there and is recognised when the forecast transaction is ultimately recognised in the profit and loss account. When a forecast transaction is no longer expected to occur, the gain or loss accumulated in the Statement of Total Recognised Gains and Losses is recognised immediately in the profit and loss account.

Pensions

The Company has obligations under two funded defined benefit pension arrangements as part of the UK Power Networks group, and the Company accounts for these schemes in accordance with FRS 17 'Retirement Benefits', ("FRS17").

The amounts charged to the profit and loss account are the current service costs and gains and losses on settlements and curtailments. Past service costs are recognised immediately in the profit and loss account if the benefits have vested. If the benefits have not vested immediately the costs are recognised over the period until vesting occurs. The interest cost and the expected return on the assets are shown as a net amount of other finance costs or credits adjacent to interest. Actuarial gains and losses are recognised immediately in the statement of total recognised gains and losses.

The defined benefit scheme is funded, with the assets of the scheme held separately from those of the Group, in a separate trustee administered fund. Pension scheme assets are measured at fair value and liabilities are measured on an actuarial basis using the projected unit method and discounted at a rate equivalent to the current rate of return on a high quality corporate bond or equivalent currency and term to the scheme liabilities. The actuarial valuations are obtained at least triennially and are updated at each balance sheet date. The resulting defined benefit asset or liability, net of the related deferred tax, is presented separately after other net assets on the face of the balance sheet.

Provisions

Provisions are recognised when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

The Company has received certain claims against the Company for work performed to date. The Company takes legal advice as to the likelihood of success of claims and actions and no provision is made where the Directors consider, based on that advice that the action is unlikely to succeed or a sufficiently reliable estimate of the potential obligation cannot be made.

NOTES TO THE FINANCIAL STATEMENTS continued

2. Turnover

Turnover, which is stated net of value added tax, arises entirely in the United Kingdom and is attributable to continuing activities of electricity distribution and the invoice value of other goods and services provided which the Directors consider represent a single class of business. This includes an estimate of the sales value of units supplied to customers between the date of the last meter reading and the year end.

3 Operating profit

	2012	2011
	£m	£m
This is stated after (crediting)/charging		
Depreciation of owned assets	70.7	66.5
(Profit)/loss on disposal of fixed assets	(0.1)	0.1
	69.6	66.6
	2012	2011
	£000	£000
Amounts payable to Auditor		
Fees payable to Company Auditor for the audit of the Company's annual accounts	35.0	33.0
Total audit fees	35.0	33.0
Other services pursuant to legislation		
- Regulatory accounts	24.3	23.3
Total non-audit fees	24.3	23.3
	59.3	56.3

The Company had no employees in either the current or the prior year.

4 Directors' emoluments

The Directors are not employed directly by the Company and did not receive any remuneration for services to the Company during the year or the preceding year.

NOTES TO THE FINANCIAL STATEMENTS continued

5 Finance charges (net)

	2012 £m	2011 £m
Interest receivable and similar income		
On loans to Group undertakings	5.6	4.0
Other interest receivable	0.2	0.8
	5.8	4.8
Interest payable and similar charges		
Net interest cost on pension scheme (note 19)	(2.5)	(1.3)
On loans from Group undertakings	(1.4)	(0.4)
On loans repayable within five years	(4.3)	(17.7)
On loans repayable after five years	(62.0)	(37.0)
Other finance charges	(1.5)	(3.8)
	(71.7)	(60.2)
Finance costs capitalised	5.5	6.8
	(66.2)	(53.4)
Fair value gains/(losses) on financial instruments		
Initial recognition of swap instruments at 26 January 2011	-	(25.8)
Gains/(losses) since initial recognition		
Fair value gains/(losses) on index linked swaps	3.1	(68.2)
Fair value (losses)/gains on interest rate swaps not qualifying for hedge accounting	(19.1)	6.3
Gains on interest rate swaps in designated fair value hedge relationships	17.2	55.5
Losses arising on adjustment for the hedged items in designated fair value hedge accounting relationships	(17.3)	(55.3)
Transfer to profit and loss on cash flow hedges	(3.2)	(0.8)
	(19.3)	(88.3)
Total finance charges (net)	(79.7)	(136.9)

Finance costs have been capitalised on the basis of a capitalisation rate of 5.9% (2011: 6.2%), which is the weighted average of rates applicable to the Company's general borrowings outstanding during the year. The cumulative interest capitalised amounts to £24.8m (2011: £19.3m).

The swap instruments were novated to the Company on 26 January 2011 from the parent UK Power Networks Holdings Limited which entered into these contracts when acquiring the Company from EDF Energy plc in October 2010.

NOTES TO THE FINANCIAL STATEMENTS continued

6. Tax on profit on ordinary activities

(a) Analysis of tax charge in the year

	2012	2011
	£m	£m
UK current tax		
UK corporation tax charge on profit for the year	12.1	10.2
Adjustment in respect of prior year	(0.7)	(4.4)
Total current tax charge (note (b))	11.4	5.8
UK deferred tax		
Origination and reversal of timing differences	14.9	2.2
Adjustment in respect of prior year	(11.7)	3.2
Effect of tax rate change on opening balance	(20.3)	(21.6)
Total deferred tax credit for the year	(17.1)	(16.2)
Total tax credit on profit on ordinary activities	(5.7)	(10.4)

(b) Factors affecting tax charge for the year

The tax assessed for the year is lower than the standard rate of corporation tax in the UK

The differences are explained below	2012	2011
	£m	£m
Profit on ordinary activities before tax	183.9	75.6
Tax on profit on ordinary activities at standard UK rate of corporation tax of 24.5% (2011: 26.5%)	45.1	20.0
Effect of		
Adjustment in respect of prior year	(0.7)	(4.4)
Disallowed expenses and non-taxable income	0.1	-
Capital allowances in excess of depreciation	(12.3)	(16.4)
Movement in short-term timing differences	(3.6)	14.0
Utilisation of tax losses	(17.2)	(7.4)
Current tax charge for the year	11.4	5.8

NOTES TO THE FINANCIAL STATEMENTS continued

6. Tax on profit on ordinary activities continued

The tax credited to the profit and loss account of £5.7m (2011: £10.4m) comprises a charge in relation to corporation tax and a credit in respect of deferred tax. The deferred tax credit has arisen due to the deferred tax liability being recalculated to take account of the reduction in the mainstream rate of corporation tax alongside a prior year adjustment that relates to increased future tax allowances on capital investment as agreed by the industry with HMRC. The effective rate of corporation tax is reduced by the availability of losses from other UK associated companies.

Tax rate changes

The 2012 Budget on 21 March 2012 announced that the UK corporation tax rate will reduce to 22% by 2014. The reduction in the rate from 26% to 24% (effective from 1 April 2012) was substantively enacted on 26 March 2012 and resulted in an average corporation tax rate for the year of 24.5%. The reduction to 23% (effective from 1 April 2013) was enacted on 3 July 2012. Remeasurement of the opening deferred tax balance at 23% reduced the deferred tax charge in the current year by £20.3m. The reduction to 22% had not been substantively enacted in Law at the balance sheet date and therefore is not relevant to these financial statements.

NOTES TO THE FINANCIAL STATEMENTS continued

7 Tangible fixed assets

	Network	Network land & buildings	Fixtures and equipment	Vehicles	Customers' contributions	Total
	£m	£m	£m	£m	£m	£m
Cost						
At 1 January 2012	4,716.0	23.4	60.4	18.5	(1,203.2)	3,615.1
Additions	283.8	2.1	15.6	0.6	(58.1)	244.0
Disposals	(18.7)	-	-	-	-	(18.7)
At 31 December 2012	4,981.1	25.5	76.0	19.1	(1,261.3)	3,840.4
Depreciation						
At 1 January 2012	1,326.1	1.6	31.7	8.8	(336.2)	1,032.0
Charge for the year	91.2	0.4	6.6	2.2	(29.7)	70.7
Disposals	(18.0)	-	-	-	-	(18.0)
At 31 December 2012	1,399.3	2.0	38.3	11.0	(365.9)	1,084.7
Net book value						
At 31 December 2012	3,581.8	23.5	37.7	8.1	(895.4)	2,755.7
At 31 December 2011	3,389.9	21.8	28.7	9.7	(867.0)	2,583.1

Network assets include land at £20.3m (2011 £20.2m). Non Network land and buildings comprises freehold buildings only.

Included within Network assets at 31 December 2012 are assets in the course of construction of £70.4m (2011 £115.5m). Approximately £83.1m of the prior year assets under construction were completed during 2012 (2011 £24.7m).

NOTES TO THE FINANCIAL STATEMENTS continued

8 Debtors

	2012 £m	2011 £m
Amounts falling due within one year		
Trade debtors	70.2	58.4
Amounts owed by Group undertakings	10.4	-
Prepayments and accrued income	9.9	9.2
	90.5	67.6
Amounts falling due after more than one year		
Amount owed by Group undertaking	145.5	145.5
Derivatives (note 12)	58.1	64.5
	203.6	210.0
	294.1	277.6

Amounts owed by Group undertakings due after more than one year represent a loan to the parent company UK Power Networks Holdings Limited which is repayable in June 2016 and incurs interest at 3.85% per annum

9 Creditors amounts falling due within one year

	2012 £m	2011 £m
Borrowings (note 11)	17.0	250.0
Amounts owed to Group undertakings	69.9	93.0
Corporation tax	5.1	7.3
Trade Creditors	0.4	-
Other creditors	3.9	4.1
Other taxation and social security	24.7	20.7
Accruals and deferred income	104.1	102.4
	225.1	477.5

10 Creditors amounts falling due after more than one year

	2012 £m	2011 £m
Borrowings (note 11)	1,488.9	1,190.7
Derivatives (note 12)	97.4	115.0
	1,586.3	1,305.7

NOTES TO THE FINANCIAL STATEMENTS continued

11. Borrowings

	2012 £m	2011 £m
Amounts falling due within one year		
Amounts due to Group undertakings	17.0	50 0
£200m 8 75% Bond due March 2012	-	200 0
	17 0	250 0
Amounts falling due after more than one year		
Revolving credit facility	120.0	-
£400m 4 75% Bond due September 2021	404.7	244 2
£350m 5 75% Bond due March 2024	349.2	349 2
£200m 8 50% Bond due March 2025	198.6	198 4
£350m 6 00% Bond due November 2036	343.8	343 6
Fair value adjustment relating to fair value interest rate swap hedges	72 6	55 3
	1,488 9	1,190 7
	1,505 9	1,440 7

Amounts due to Group undertakings comprise a loan from a fellow subsidiary carrying interest at 1 31% per annum and repayable in March 2013

Funds drawn under the revolving credit facility bear interest at 1 2% per annum This is part of a £210 0m facility provided by a syndicate of banks which is available until February 2017

The carrying value of the bonds is net of unamortised issue costs of £8 4m (2011 £14 7m) and includes an unamortised premium on the 4 75% bond of £4 7m (2011 £nil) These balances together with the interest expense are allocated to the profit and loss account over the term of the debt

In March 2012 the Company raised an additional £150 0m through a tap issue on the existing 4 75% £250 0m bond facility maturing in September 2021 The resulting £400 0m nominal value carries a net premium of £4 7m as a result of a favourable shift in market prices at the time of the tap issue

Fair value adjustments increasing the carrying amount of the bonds by £17 3m (2011 £55 3m) were booked through the profit and loss account during the year These relate to the fair value movement in interest rate swaps designated as fair value hedges The cumulative fair value adjustment on the bonds at 31 December 2012 of £72 6m (2011 £55 3m) is presented on a separate line in the table above

No security has been given over the assets of the Company in respect of external debt or amounts owed to Group undertakings

NOTES TO THE FINANCIAL STATEMENTS continued

12. Derivative financial instruments

	2012 £m	2011 £m
Derivative financial assets		
Interest rate swaps designated as effective fair value hedges	37.2	20.0
Interest rate swaps that are not designated in hedge accounting relationships	20.9	44.5
	58.1	64.5
Derivative financial liabilities		
Index linked swaps	(68.2)	(84.3)
Interest rate swaps that are not designated in hedge accounting relationships	(29.2)	(30.7)
	(97.4)	(115.0)
	(39.3)	(50.5)

The Company exited a number of swap arrangements on 20 November 2012. Proceeds arising from the termination of 'in the money' interest rate swaps contributed toward the settlement of 'out of the money' RPI index linked swap positions.

Cash settlement of the fair value on 20 November 2012 amounted to £3.0m for interest rate swaps not designated in hedge accounting relationships offset by £13.0m payable on the RPI index linked swaps. Together with interest receivable and transaction fees the net payment required to exit these contracts was £2.4m.

Further details of derivative financial instruments are provided in Note 13.

13. Financial instruments

Risk management

The Company's funding, liquidity and exposure to interest rate risk is managed by the immediate parent company, UK Power Networks Holdings Limited. Treasury operations are conducted within a framework of policies and guidelines authorised by the Board of UK Power Networks Holdings Limited.

(a) Interest rate and currency risk

A number of swaps have been transacted to change the interest rate exposure of the Company to include an appropriate mix of fixed, floating and RPI linked interest rates.

The Company does not have any direct material exposure to foreign currencies.

NOTES TO THE FINANCIAL STATEMENTS continued

13 Financial instruments continued

(b) Interest rate swap contracts

Under interest rate swap contracts, the Company agrees to exchange the difference between fixed and floating rate interest calculated on agreed notional principal amounts. The fair value of interest rate swaps at the reporting date is determined by discounting the future cash flows implicit in the swaps.

The following tables and discussion detail the notional principal amounts, the fair values and remaining terms of interest rate swap contracts outstanding as at the reporting date.

Fair value hedges

	Average contract fixed		Notional principal		Fair value	
	interest rate		value			
	2012	2011	2012	2011	2012	2011
	%	%	£m	£m	£m	£m
Outstanding receive fixed/ pay floating contracts	7.2%	7.2%	380.0	380.0	37.2	20.0

The floating rate payable on the interest rate swaps is six month LIBOR plus a margin of between 2.1% and 4.8%. The maturity dates of the swaps range between March 2024 and March 2025. Interest payable is settled on a semi-annual basis and interest receivable on an annual basis.

The swaps exchange fixed rate interest for floating rate interest and were effective as fair value hedges throughout the year in respect of bond interest rates. Fair value gains during the year of £17.2m (2011: £55.5m) are offset by fair value losses of £17.3m (2011: £55.3m) adjusted to the carrying amount of the bonds through the profit and loss account.

NOTES TO THE FINANCIAL STATEMENTS continued

13. Financial Instruments continued

(b) Interest rate swap contracts continued

Interest rate swaps not designated in hedge accounting relationships

The Company is party to a number of interest rate swap contracts, not designated in hedge accounting relationships, with fair values amounting to assets of £20.9m (2011: £44.5m) and liabilities of £29.2m (2011: £30.7m). The swap arrangements are as follows:

- I The fair value swap contracts described in the preceding section which exchange fixed for floating rates of interest on a notional principal of £380.0m are overlaid by £200.0m of additional swap contracts which re-fix the floating rates of interest to fixed rates until the next regulatory price control review in March 2015. The resulting fixed rate is on average 0.8% lower than the underlying bond coupon rate.
- II A swap contract was entered into as a pre-hedge to the issue of new bond debt in 2011, swapping 6 month Libor to a fixed rate of 2.99%. The swap was designated as a cash flow hedge until the issue of the bonds in September 2011 at which point it was de-designated from the hedge relationship and subsequent gains or losses recognised immediately in the profit or loss. Whilst the instrument was effective as a cash flow hedge, a loss of £18.3m was deferred to the cash flow hedge reserve. This loss is being amortised to the profit and loss account over the life of the swap instrument. During the year £3.2m (2011: £0.8m) was released to the profit and loss from the cash flow hedge reserve.

At the time of the bond issue a mirror swap was transacted to offset the effect of the original swap by swapping 1.73% fixed interest with 6 month Libor. The ongoing net effect of both instruments is 1.26% fixed interest on a notional principal of £220.0m until March 2017.

(c) Index linked swap contracts not designated in hedge accounting relationships

The Company uses RPI linked swap contracts to convert a portion of the fixed rate interest payable under the bonds to an inflation linked rate. Although designed as an economic hedge against the RPI exposure of the Company's regulated income these instruments are not designated in formal hedge accounting relationships. The index linked swaps receive a combination of fixed and floating rate interest and pay RPI linked interest on a notional value of £500.0m (2011: £570.0m). On 20 November 2012 the Company paid £13.0m to exit one contract with a notional value of £70m and maturing in March 2024 (note 12). Maturity dates of the remaining contracts range from November 2036 to December 2041. At 31 December 2012 the fair value of these instruments was £68.2m out of the money (2011: £84.3m).

NOTES TO THE FINANCIAL STATEMENTS continued

13. Financial Instruments continued

(d) Interest rate profile

Interest earned on cash deposits is predominantly through money market investments. Money market investments are short term in nature and taken out at fixed rates of interest for the duration of the investment.

After taking into account the Company's interest rate and index linked swaps, the interest rate profile of the Company's financial liabilities is as follows:

	Borrowings			Total £m	Fixed rate borrowings	
	Floating rate £m	Index linked £m	Fixed rate £m		Weighted average fixed rate %	Weighted average fixed period Years
As at 31 December 2012	120.0	495.6	890.3	1,505.9	6.1	7.9
As at 31 December 2011	-	418.4	1,022.3	1,440.7	6.1	7.2

The index linked rates range from 1.7% to 1.95% indexed by RPI over the period of the relevant instrument. The combined weighted average cost of floating, index linked and fixed rate borrowings for the year was 5.8% (2011: 6.2%).

(e) Fair values

The fair values of financial instruments represent the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation.

The Company's borrowings recorded at amortised cost are shown below together with the fair value:

	Book value 2012 £m	Fair value 2012 £m	Book value 2011 £m	Fair value 2011 £m
Amounts payable				
Within one year	17.0	17.0	250.0	253.3
In two to five years	120.0	120.0	-	-
In more than five years	1,368.9	1,596.7	1,190.7	1,350.4
	1,505.9	1,733.7	1,440.7	1,603.7

The fair value of the bonds has been determined by reference to closing quoted market values where available or otherwise by discounting future cash flows at their market interest rate. The fair value of all other financial assets and liabilities approximates to their carrying value.

(f) Borrowing facilities

The Company has access to a revolving credit facility of £210.0m until February 2017, of which £120.0m was drawn at 31 December 2012.

NOTES TO THE FINANCIAL STATEMENTS continued

14 Provision for liabilities

The movements in provisions during the current year are as follows

	At 1 January 2012 £m	Arising during the year £m	Released during the year £m	At 31 December 2012 £m
Deferred tax	263.2	-	(16.8)	246.4
Other	2.2	4.4	(0.2)	6.4
	265.4	4.4	(17.0)	252.8

“Other” comprises provisions for legal fees which are expected to become payable within the next year

Deferred taxation provided in the financial statements is as follows

	2012 £m	2011 £m
Accelerated capital allowances	263.9	286.0
Other timing differences	(17.5)	(22.8)
Provision for deferred tax	246.4	263.2

The movements in deferred taxation are as follows

	At 1 January 2012 £m	Profit and loss account £m	Statement of total recognised gains and losses £m	At 31 December 2012 £m
Provision for deferred tax	263.2	(17.8)	1.0	246.4
Deferred tax shown against pension liability	(20.2)	0.7	1.7	(17.8)
Net deferred tax	243.0	(17.1)	2.7	228.6

NOTES TO THE FINANCIAL STATEMENTS continued

15. Share capital

Authorised

	2012	2011	2012	2011
	Number	Number	£m	£m
Ordinary shares of £0.50 each	400,000,000	400,000,000	200.0	200.0

Allotted, called up and fully paid

	2012	2011	2012	2011
	Number	Number	£m	£m
Ordinary shares of £0.50 each	251,513,142	251,513,142	125.8	125.8

16 Dividends paid

	2012	2011
	£m	£m
Ordinary dividends on equity shares – 21.87p (2011: 29.82p) per ordinary share	55.0	75.0

NOTES TO THE FINANCIAL STATEMENTS continued

17 Reconciliation of shareholder's funds

	Share Capital £m	Share premium account £m	Capital redemp- tion reserve £m	Hedging Reserve £m	Profit and loss account £m	Total Share holder's funds £m
At 1 January 2011	125.8	5.6	10.6	-	694.3	836.3
Profit for the year	-	-	-	-	86.0	86.0
Dividends paid	-	-	-	-	(75.0)	(75.0)
Actuarial loss net of deferred tax on defined pension benefits	-	-	-	-	(24.4)	(24.4)
Deferred tax rate change	-	-	-	-	(1.4)	(1.4)
Losses on cashflow hedges net of deferred tax	-	-	-	(13.7)	-	(13.7)
Transfer to profit or loss on cash	-	-	-	0.6	-	0.6
At 31 December 2011	125.8	5.6	10.6	(13.1)	679.5	808.4
Profit for the year	-	-	-	-	189.6	189.6
Dividends paid	-	-	-	-	(55.0)	(55.0)
Actuarial gain net of deferred tax on defined pension benefits	-	-	-	-	0.1	0.1
Deferred tax rate change	-	-	-	(0.3)	(1.7)	(2.0)
Transfer to profit or loss on cash flow hedges net of deferred tax	-	-	-	2.5	-	2.5
At 31 December 2012	125.8	5.6	10.6	(10.9)	812.5	943.6

The losses deferred to the hedging reserve relate to an interest rate swap entered into as a pre hedge to the issue of new bond debt in 2011. The swap was designated as an effective cash flow hedge until the issue of the bonds at which time hedge accounting was discontinued and subsequent gains or losses on the instrument recognised immediately in the profit or loss account. The hedge reserve is amortised to the profit and loss over the life of the instrument.

NOTES TO THE FINANCIAL STATEMENTS continued

18. Financial commitments

Amounts contracted for but not provided in the financial statements amounted to £47.7m (2011 £56.9m)

19. Pension commitments

The Group operates two funded defined benefit pension schemes

- The UK Power Networks Group of the ESPS (the UKPN Group) – formerly the Networks Section of the EDF Energy Group of the Electricity Supply Pension Scheme (ESPS), and
- The UK Power Networks Pension Scheme (UKPNPS) – formerly the Networks Section of the EDF Energy Pension Scheme (EEPS)

The parent company UK Power Networks Holdings Limited assumed responsibility for these defined benefit arrangements when it acquired the Distribution Networks businesses and associated unregulated businesses from the former parent company EDF Energy plc on 29 October 2010. Scheme assets and liabilities were assigned to the individual legal entities of the Group, including this Company, using a revised allocation methodology based on the attribution portions agreed with the industry regulator Ofgem, within the latest price control determination, DPCR5.

The actuarial valuation at 31 December 2012 was carried out by Aon Hewitt. The most recent independent triennial valuation of the schemes for funding purposes was performed as at 31 March 2010. Under the funding schedule agreed with the scheme trustees, the Group aims to eliminate the current deficit over the next 14 years. The Group will monitor funding levels annually and the funding schedule will be reviewed between the Group and the trustees every three years based on actuarial valuations. The next independent triennial valuation is due to be completed at 31 March 2013. The Group considers that the contributions rates agreed with the trustees are sufficient to eliminate the current deficit over the agreed period.

NOTES TO THE FINANCIAL STATEMENTS continued

19. Pension commitments continued

The principle financial assumptions (% per annum) used to calculate scheme liabilities under FRS17 were

	2012	2011
	%	%
Discount rate		
- UKPN Group	4.3	4.6
- UKPNPS	4.8	4.7
Expected return on scheme assets		
- UKPN Group	4.6	4.8
- UKPNPS	5.8	5.8
Rate of increase in RPI		
- UKPN Group	2.8	3.0
- UKPNPS	3.1	3.3
Rate of increase in CPI		
- UKPN Group	2.3	2.1
- UKPNPS	2.6	2.4
Rate of increase in salaries		
- UKPN Group	3.8	4.0
- UKPNPS	4.1	4.3
Rate of pension increases in payment		
- Pensions in excess of GMP (UKPN Group)	2.9	3.0
- Post 88 GMP (UKPN Group)	1.9	1.8
- RPI up to 5% per annum (UKPNPS)	2.9	3.0
- RPI up to 2.5% per annum (UKPNPS)	2.0	2.0
- Post 88 GMP (UKPNPS)	2.0	1.9
Rate of pension increases in deferment		
- UKPN Group	2.9	3.0
- CPI up to 5% per annum (UKPNPS)	2.6	2.4
- CPI up to 2.5% per annum (UKPNPS)	2.5	2.4

NOTES TO THE FINANCIAL STATEMENTS continued

19. Pension commitments continued

The table below shows details of assumptions around mortality rates used to calculate the FRS 17 pension liabilities

	At 31 December 2012 years	At 31 December 2011 years
UKPN Group		
Life expectancy for current male pensioner aged 60	28	28
Life expectancy for current female pensioner aged 60	30	30
Life expectancy for future male pensioner from age 60 retiring in 2030	30	30
Life expectancy for future female pensioner from age 60 retiring in 2030	32	32

UKPNPS

Life expectancy for current male pensioner aged 65	22	22
Life expectancy for current female pensioner aged 65	24	24
Life expectancy for future male pensioner from age 65 retiring in 2030	24	24
Life expectancy for future female pensioner from age 65 retiring in 2030	27	27

These assumptions are governed by FRS 17 and do not reflect the assumptions used by the independent actuary in the triennial valuation as at 31 March 2010, which determined the Company's contribution rate for future years

The amount recognised in the balance sheet in respect of the Company's defined benefit retirement benefit plan is as follows

	UKPN Grp 2012 £m	UKPNPS 2012 £m	Total 2012 £m	Total 2011 £m
Fair value of scheme assets	365.8	32.9	398.7	368.7
Present value of defined benefit obligations	(438.6)	(37.6)	(476.2)	(449.5)
Deficit in scheme	(72.8)	(4.7)	(77.5)	(80.8)
Related deferred tax asset	16.7	1.1	17.8	20.2
Liability recognised in the balance sheet	(56.1)	(3.6)	(59.7)	(60.6)

This amount is presented in pension liabilities

NOTES TO THE FINANCIAL STATEMENTS continued

19. Pension commitments continued

Amounts recognised in the profit and loss account in respect of the defined benefit schemes are as follows

	UKPN Grp 2012 £m	UKPNPS 2012 £m	Total 2012 £m	Total 2011 £m
Current service cost	(10.8)	(5.1)	(15.9)	(15.0)
Changes in respect of terminations	(2.6)	-	(2.6)	(2.3)
Interest cost	(18.7)	(1.7)	(20.4)	(19.3)
Expected return on scheme assets	16.2	1.7	17.9	18.0
	(15.9)	(5.1)	(21.0)	(18.6)

Of the charge for the year £18.5m (2011: £17.3m) has been included in distribution costs and an expense of £2.5m (2011: £1.3m) has been included in interest payable. The estimated amounts of contributions expected to be paid to the scheme in 2013 is £22.1m.

Movements in the present value of defined benefit obligations in the current year were as follows

	UKPN Grp 2012 £m	UKPNPS 2012 £m	Total 2012 £m	Total 2011 £m
At 1 January	(416.0)	(33.5)	(449.5)	(351.3)
Current service cost	(10.8)	(5.1)	(15.9)	(15.0)
Changes in respect of terminations	(2.6)	-	(2.6)	(2.3)
Interest cost	(18.7)	(1.7)	(20.4)	(19.3)
Actuarial (loss)/gain	(10.0)	4.1	(5.9)	(75.4)
Benefits paid/(received)	19.5	(1.4)	18.1	13.8
At 31 December	(438.6)	(37.6)	(476.2)	(449.5)

The actuarial loss includes a net transfer out of scheme liabilities amounting to £11.0m (2011: £55.7m transfer in) to align the allocation of scheme liabilities across the Group to the attribution portions agreed with the Regulator under the latest price control determination DPCR5.

NOTES TO THE FINANCIAL STATEMENTS continued

19. Pension commitments continued

Movements in the present value of fair value of scheme assets in the current year were as follows

	UKPN Grp 2012 £m	UKPNPS 2012 £m	Total 2012 £m	Total 2011 £m
At 1 January	343.3	25.4	368.7	300.0
Expected return on scheme assets	16.2	1.7	17.9	18.0
Actuarial gain	6.0	-	6.0	42.8
Contributions by employer	12.1	3.5	15.6	15.1
Deficit payments	7.7	0.9	8.6	6.6
Benefits (paid)/received	(19.5)	1.4	(18.1)	(13.8)
At 31 December	365.8	32.9	398.7	368.7

The actuarial gain includes a net transfer out of scheme assets amounting to £9.6m (2011 £45.4m transfer in) to align the allocation of scheme assets across the Group to the attribution portions agreed with the Regulator under the latest price control determination DPCR5

The analysis of the scheme assets and the expected rate of return at the balance sheet date were as follows

	Expected return		Fair value of assets			
	2012 %	2011 %	UKPN Grp 2012 £m	UKPNPS 2012 £m	Total 2012 £m	Total 2011 £m
Gilts - fixed	2.7	2.8	88.1	-	88.1	85.2
- index linked	2.4	2.7	75.6	-	75.6	78.9
Equities	7.9	7.9	125.9	14.9	140.8	134.5
Property	6.9	6.9	11.8	2.6	14.4	16.2
Corporate bonds	4.1	4.7	39.9	12.9	52.8	23.3
Hedge Funds	4.1	4.7	7.7	-	7.7	5.6
Cash	0.5	1.1	16.8	2.5	19.3	25.0
			365.8	32.9	398.7	368.7

The Group employs a building block approach in determining the long-term rate of return on pension plan assets. Historical markets are studied and assets with higher volatility are assumed to generate higher returns consistent with widely accepted capital market principles. The assumed long-term rate of return on each asset class is set out in the table above. The overall expected rate of return as presented in the assumptions table on page 31 is derived by aggregating the expected return for each asset class over the actual asset allocation for each of the schemes as at 31 December 2012.

The actual return on scheme assets in the year was a gain of £33.5m (2011 £15.4m)

NOTES TO THE FINANCIAL STATEMENTS continued

19. Pension commitments continued

The history of experience gains and losses is as follows

	2012 £m	2011 £m	2010 £m	2009 £m	2008 £m
Fair value of scheme assets	398.7	368.7	300.0	182.9	164.6
Present value of defined benefit obligations	(476.2)	(449.5)	(351.3)	(238.2)	(179.4)
Deficit in the scheme	(77.5)	(80.8)	(51.3)	(55.3)	(14.8)

Experience adjustments on scheme liabilities

Amount (£m)	(6.8)	(2.2)	(2.6)	(1.9)	(0.7)
Percentage of scheme liabilities (%)	1.4	0.5	0.7	0.8	0.4

Experience adjustments on scheme assets

Amount (£m)	15.6	(2.6)	13.0	14.9	(44.9)
Percentage of scheme assets (%)	3.9	0.7	4.3	8.2	27.3

The amounts recognised in the statement of total recognised gains and losses are as follows

	UKPN Grp 2012 £m	UKPNPS 2012 £m	Total 2012 £m	Total 2011 £m
At 1 January	(70.6)	(5.4)	(76.0)	(50.2)
Actuarial (loss)/gain	(4.0)	4.1	0.1	(32.6)
Deferred taxation	0.9	(0.9)	-	8.2
Deferred tax rate change	(1.5)	(0.2)	(1.7)	(1.4)
At 31 December	(75.2)	(2.4)	(77.6)	(76.0)

The cumulative amount of actuarial gains and losses recognised in the statement of total recognised gains and losses since the adoption of FRS 17 is a loss of £77.6m (2011: £76.0m)

20. Related parties

In accordance with FRS 8 'Related party disclosures', the Company is exempt from disclosing transactions with entities that are part of the Group or investees of the Group qualifying as related parties, as it is a wholly owned subsidiary of a parent, which prepares consolidated accounts which are publicly available

NOTES TO THE FINANCIAL STATEMENTS continued

21 Parent undertaking and controlling party

The Company is a wholly owned subsidiary of UK Power Networks Holdings Limited, a company registered in England and Wales

UK Power Networks Holdings Limited is owned by a consortium consisting of

Power Assets Holdings Limited	Incorporated in Hong Kong
Li Ka Shing Foundation Limited	Incorporated in Hong Kong
Cheung Kong Infrastructure Holdings Limited	Incorporated in Bermuda

It is the opinion of the Directors that the parent company, UK Power Networks Holdings Limited has no single controlling party as that company is controlled jointly by the consortium. The UK Power Networks Holdings group is both the smallest and largest group for which consolidated financial statements are prepared which include the results of the Company. Copies of the financial statements of UK Power Networks Holdings Limited may be obtained from the Company Secretary at Energy House, Carrier Business Park, Hazelwick Avenue, Three Bridges, Crawley, West Sussex, RH10 1EX

22. Regulatory accounts

On 1 October 2001, under the Utilities Act 2000, Eastern Power Networks plc was granted a Distribution Licence under which it is required to produce regulatory accounts. The regulatory accounts, which cover a 12 month period ended 31 March of each year, are available free of charge by contacting the Finance Department at Energy House, Carrier Business Park, Hazelwick Avenue, Three Bridges, Crawley, West Sussex, RH10 1EX or by telephoning 01293 657862