

Registered number: 3600574

**WESTERN POWER DISTRIBUTION (WEST MIDLANDS) plc**

**ANNUAL REPORT AND FINANCIAL STATEMENTS**

**For the year ended 31 March 2013**

Western Power Distribution (West Midlands) plc is an integral part of a larger UK group. The structure of the group is such that the financial statements of Western Power Distribution (West Midlands) plc must be read in conjunction with the group financial statements of PPL WEM Holdings plc to gain a full understanding of the group results for the year and the related cash flows, together with the financial position of the group as at 31 March.



**WESTERN POWER**  
**DISTRIBUTION**

*Serving the Midlands, South West and Wales*

---

## **Contents**

	<b>Page</b>
<b>Directors' report</b>	<b>1</b>
<b>Statement of directors' responsibilities</b>	<b>16</b>
<b>Independent auditors' report to the members of Western Power Distribution (West Midlands) plc</b>	<b>17</b>
<b>Financial statements:</b>	
Profit and loss account	19
Statement of total recognised gains and losses	20
Balance sheet	21
Statement of cash flows	22
Notes to the statement of cash flows	23
Notes to the financial statements	25

---

## **Directors' report**

For the year ended 31 March 2013

The directors present their report and the audited financial statements of Western Power Distribution (West Midlands) plc (previously known as Central Networks West plc) (the "Company" or "WPD West Midlands"), company number 3600574, for the year ended 31 March 2013. As the financial statements for the current period are for 12 months and the comparatives are for 15 months, then they are not directly comparable. Non financial information in the Directors' report is presented on a regulatory year to 31 March basis.

**WPD West Midlands is an integral part of a larger UK group. The structure of the group is such that the financial statements of the Company must be read in conjunction with the group financial statements of PPL WEM Holdings plc ("PPL WEM") to gain a full understanding of the group results for the year and the related cash flows, together with the financial position of the group as at 31 March 2013.**

### **Principal activity**

WPD West Midlands' principal activity is the distribution of electricity within its authorised area covering the West Midlands region of England.

The principal activity of the PPL WEM Holdings plc group ("WEM Group") is the distribution of electricity across its networks in the Midlands region of England. The WEM Group is structured so as to minimise the costs of debt. Interest payments on the debt held by WEM Group companies other than WPD West Midlands and Western Power Distribution (East Midlands) plc ("WPD East Midlands"), together with certain other items, are funded primarily through dividend payments from WPD West Midlands and WPD East Midlands (together "WPD Midlands"). WPD Midlands was previously known as Central Networks.

PPL WW Holdings Limited, an affiliate of PPL WEM, is the owner of Western Power Distribution (South West) plc ("WPD South West") and Western Power Distribution (South Wales) plc ("WPD South Wales"). The principal activity of the PPL WW Holdings Limited group ("WW Group") is the distribution of electricity across South West England and South Wales.

The WW Group and WEM Group collectively trade as Western Power Distribution ("WPD"). The management of the WW Group is involved in the management of the network in the South West, South Wales and the Midlands areas of England and, where appropriate, they share engineering control and other systems.

### **Ownership**

WPD West Midlands is an indirect, wholly-owned subsidiary of PPL WEM Holdings plc which is owned by PPL Corporation, an electricity utility of Allentown, Pennsylvania, United States of America ("US").

### **Business review**

WPD West Midlands is a monopoly regulated by licence and operates under a price control regime. WPD West Midlands' distribution licence authorises it to distribute electricity in an area covering the West Midlands, including such areas as Gloucestershire, Worcestershire, Stoke and the UK's second largest city, Birmingham. WPD West Midlands' network comprises approximately 23,850 km of overhead lines and 42,844 km of underground cable providing an electricity supply to 2.5 million end users.

During 2012/13, the maximum demand recorded was 4,796 megawatts (2011/12 4,767 megawatts).

## **Directors' report (continued)**

For the year ended 31 March 2013

### **Business review (continued)**

The operations of WPD West Midlands are regulated under its distribution licence under which income is generated subject to a price cap regulatory framework that provides economic incentives to minimise operating, capital and financing costs. The charges made for the use of the distribution network are regulated on the basis of the Retail Price Index ("RPI") plus/minus X formula where RPI is a measure of inflation and X is an efficiency factor established by the regulator following review. The regulator, known as Ofgem, currently sets the distribution price control formula for five year periods.

The electricity distribution price control review for the five year period which commenced on 1 April 2010 ("DPC5") was agreed with Ofgem in December 2009. Ofgem's proposal for DPC5 broadly focuses on environment, customers and networks and this fits closely with our own business strategy. WPD West Midlands will be allowed to increase its prices by an average of 4.3% plus inflation in each of the five years of DPC5. In 2013/14, allowed revenues will be reduced by approximately £11m in respect of a line losses incentive relating to the previous review period (DRC4), see Note 20c). In return for the revenue WPD West Midlands will be allowed to earn in this period, Ofgem introduced from 1 April 2010 new obligations in areas such as connection performance together with incentives to innovate and reduce both the number of interruptions that our customers suffer and the average length of interruptions.

In October 2010, Ofgem completed a comprehensive review of the 20 year old framework of monopoly network regulation. They introduced a new approach for sustainable network regulation, to be delivered by the "RIIO" model where  $\text{Revenue} = \text{Incentives} + \text{Innovation} + \text{Outputs}$ . Under the RIIO model there will be a much greater emphasis on companies playing a full role in developing a more sustainable energy sector and delivering value for money network services for customers. A key feature of the RIIO model is that the setting of outputs that network companies are expected to deliver will be much more extensive with the outputs embedded within the overall business plan and act as a "contract" between the network companies and their customers. WPD West Midlands' next price review (known as RIIO-ED1), effective from 1 April 2015 and which is expected to apply for eight years, will embody these principles.

In February 2012 Ofgem launched the start of RIIO-ED1, the first electricity distribution price control review under RIIO. Following a strategy consultation published in September 2012, Ofgem published its Strategy Decision in March 2013. WPD has been actively engaged in developing the outputs based Business Plan and shaping the RIIO-ED1 framework within which the Plan will be assessed.

The focus for the business during the year has been to concentrate on the five key goals of safety, network reliability, customer service, environment and business efficiency. Operationally, WPD has completed another successful year and continues to be a frontier performer in terms of network reliability despite some challenging weather conditions. Ofgem acknowledged the WW Group's exceptional operating performance during the DPC5 review process where the WW Group's strong performance within the sector was rewarded for both capital efficiency and service delivery; this strong performance is now being evidenced in the WEM Group DNOs (see "Network Performance"). As we now focus on our plans for the next price control review and submitting a well justified business plan, a vital aspect of this is to demonstrate an excellent track record of operational delivery throughout the DPC5 period, meeting and surpassing the targets agreed.

A combination of targeted investment and close monitoring of performance has ensured that we have outperformed in all areas of the business. WPD West Midlands during the year recorded just two failures against Ofgem's national Customer Guarantee Service Standards for network performance, and two failures for the year against the 37 standards relating to connections performance. We also exceeded all of our network performance targets under the Quality of Service incentive scheme by a significant margin.

## **Directors' report (continued)**

For the year ended 31 March 2013

### **Business review (continued)**

#### ***Safety***

The safety of our staff, customers and members of the public continues to be a core value at the heart of all our business operations. Maintaining a practical and pragmatic safety culture from the "top down" remains an imperative. WPD staff continue to play an active role in many national committees and steering groups which concentrate on the future of safety and training policies across the industry.

The number of lost time accidents to staff working in WPD West Midlands was 6 in 2012/13. This compares with 1 reported in 2011/12 and 12 reported in 2010/11.

The number of non-lost time accidents to staff working in WPD West Midlands was 57 in 2012/13. This compares with 43 reported in 2011/12. The total number of accidents across WPD as a whole unfortunately rose to 133 in 2012/13 from 120 in 2011/12.

The integration of WPD Midlands into the WPD Safety Management System was the most significant safety related activity during 2012/13.

Following the acquisition in April 2011, the Safety Team focused on the following areas of work:

- continue to support WPD South West and WPD South Wales staff to maintain a clear focus on safety
- support and assist WPD Midlands staff to develop and maintain a clear "WPD style" focus on safety through a period of significant organisational change and upheaval
- carry out a gap analysis of the differences between WPD and Central Networks Safety Management Systems, so that additions and changes could be identified and implemented
- reorganisation of the Central Networks Safety and Training Team into the WPD structure
- delivery of training to WPD Midlands staff on general and operational safety rules and procedures
- introduction of existing WPD procedures into WPD Midlands within 12 months of acquisition

The WPD Distribution Safety Rules ("DSRs") and authorisations, together with WPD operational and general health and safety policy, were introduced successfully into WPD Midlands in March 2012 after the Safety Team delivered more than 250 local briefing sessions. At the same time, new DSRs were introduced into WPD South West and WPD South Wales.

WPD Midlands Team Managers and Distribution Managers have been actively supported in the new safety responsibilities during one-to-one visits by members of the Safety Team.

In December 2012, a formal audit concluded that the combined Safety Management Systems conforms to OHSAS 18801:2007.

A new arc and flame retardant clothing policy has been introduced into the Company.

During the autumn, members of the Safety Team visited all WPD depots for face-to-face sessions with staff entitled "Safety Fundamentals" focusing on the basics of PPE (personal protective equipment) and compliance with the principles of WPD Policy.

## Directors' report (continued)

For the year ended 31 March 2013

### Business review (continued)

#### Safety (continued)

There was one formal Improvement Notice invoked against WPD by the Health & Safety Executive ("HSE") during 2012/13. This notice was issued following an audit in which a number of low voltage ("LV") overhead lines were found to be below the statutory minimum ground clearance of 5.8m across roadways. Actions are currently being undertaken to comply with this notice. These actions include:

- revisions to WPD Overhead Inspection Policy to include the recording of line heights on CROWN (WPD's capital system), audit of inspection outputs and the introduction of a task-specific authorisation and computer based competence check
- a sample check of LV overhead line road crossings across all four of WPD's licence areas
- a training session for all WPD overhead line inspection staff and contractors.

#### Network performance

Performance of the distribution network is measured in two key ways:

Security - the number of supply interruptions recorded per 100 connected customers ("CI"), and

Availability - the number of customer minutes lost per connected customer ("CML")

All licensees who operate a distribution system are required to report annually to Ofgem on their performance in maintaining system Security and Availability. The Quality of Service incentive scheme, also known as the Information and Incentives Scheme ("IIS") which was introduced by Ofgem in April 2002, financially incentivises all licensees including WPD with respect to both the Security and Availability of supply delivered to customers.

Network performance reported to Ofgem for the regulatory year to 31 March was as follows:

	<u>Total</u>	<u>Target (less than)</u>
Minutes lost per customer 2012/13	46.1	
Excluded events	(1.3)	
<b>IIS Performance 2012/13</b>	<b>44.8</b>	<b>95.6</b>
IIS Performance 2011/12	49.0	96.3
IIS Performance 2010/11	89.5	97.0
Interruptions per 100 customers 2012/13	82.9	
Excluded events	(1.5)	
<b>IIS Performance 2012/13</b>	<b>81.4</b>	<b>109.9</b>
IIS Performance 2011/12	73.7	109.9
IIS Performance 2010/11	102.2	109.9

The figures above cover all reportable interruptions longer than three minutes in duration occurring on the WPD West Midlands network including those caused by bad weather and other faults together with 50% of CI and CML due to pre-arranged shutdowns for maintenance and construction. The 11kV network is the principal driver of customer minutes lost, with faults on overhead lines being the major contributor. In addition to the performance reported under IIS above, 88.1% of customers off supply in the West Midlands as the result of a high voltage ("HV") fault were restored within one hour of the fault occurring.

## **Directors' report (continued)**

For the year ended 31 March 2013

### **Business review (continued)**

#### ***Network performance (continued)***

Under the IIS scheme, performance is targeted at an underlying level of improvement. Distribution Network Operators ("DNOs") are thus permitted to claim an adjustment for events during the year which they believe were exceptional and had a significant impact on the total reported performance. An exceptional event can either be caused by a large number of weather related faults or be due to a one-off event which is outside of the DNO's control. In either case, the event must meet prescribed thresholds in terms of the number of faults experienced or, for a one-off event, in terms of either the number of customers affected or the duration of the incident. If an event meets these prescribed thresholds, the DNO must notify Ofgem who will conduct an audit to determine the impact of the event. As part of the audit process the DNO must demonstrate that it mitigated against the impact of the event to the best of its ability before Ofgem will exclude the CI and CML incurred. WPD West Midlands reported one exceptional event to Ofgem during the year.

Subject to Ofgem confirmation, our IIS CML and CI of 44.8 customer minutes lost and 81.4 interruptions per 100 customers for the year are within our targets of 95.6 and 109.9 respectively. WPD will continue with those initiatives that have clearly demonstrated good improvements to quality of supply to date, and will seek new opportunities and initiatives for the future. Our focus for 2013/14 and beyond will be to further reduce interruptions by progressing an ongoing programme to increase the automation of the HV network.

#### ***Customer service***

We are committed to providing excellent customer service at all times and strongly believe that customer satisfaction is the key to the future success of the business. When dealing with customers our policy is to get it right "first time, every time". On the occasions when we fail to meet this standard, staff are encouraged to take personal responsibility for customer issues, to follow the problem through to the end, and to adopt our golden rule – "treat customers the way that we would like to be treated".

If customers are not happy with our efforts to resolve their complaint, they have historically been able to ask the statutory body, the Gas and Electricity Consumer Council (known as "energywatch"), to review the matter. Until 30 September 2008, when energywatch was disbanded, energywatch had received no complaints in respect of WPD West Midlands since January 2005. energywatch was replaced by The Energy Ombudsman ("Ombudsman") with effect from 1 October 2008. WPD South West and WPD South Wales achieved a fourth year of the statutory Energy Ombudsman Scheme with zero customer complaints. WPD East and West Midlands also achieved a complaint-free year for the first time.

We have developed a good working partnership with the Ombudsman to identify potential customer issues and resolve them before they develop into customer complaints. Regular meetings between WPD and the Ombudsman have resulted in a number of initiatives to improve our overall service to customers and drive standards up. WPD South Wales and WPD South West are the only network companies to have zero complaints referred to the Ombudsman during the first four years of operation of the statutory scheme.

#### **Discretionary Reward Scheme**

For 2012/13 Ofgem replaced the Discretionary Reward Scheme with a Stakeholder Award Scheme (which is a key element of Ofgem's new Broad Measure of Customer Satisfaction). This was piloted in 2012/13 which meant that no monetary incentive was awarded. Only three of the six DNO groups met the minimum requirements (based on written submissions). Of these WPD was awarded the highest score of 8.6 out of 10 for the overall submission which included a question and answer session with the judging panel.

## **Directors' report (continued)**

For the year ended 31 March 2013

### **Business review (continued)**

#### ***Customer service (continued)***

##### **Broad Measure of Customer Satisfaction**

From April 2012, the Broad Measure of Customer Satisfaction Incentive replaced the telephone customer service survey incentive. A research agency undertakes a monthly satisfaction survey of DNO customers who contact the DNO to report loss of supply, have a general enquiry or request a new connection. As at March 2013, the four WPD DNOs were ranked joint 1st place (WPD South Wales and WPD South West), 3rd place (WPD East Midlands) and 5th place (WPD West Midlands) in the league table of all DNOs for the new incentive matrix.

Ofgem also compared the speed of response that a DNO call centre provides and WPD was identified as a top performer with an average speed of response below two seconds compared to a national average of 13.3 seconds.

##### **National Customer Service Excellence Standard**

WPD have been fully reaccredited to the Customer Service Excellence Standard including WPD Midlands for the first time. The assessor visited a number of locations across WPD and was particularly complimentary of the achievements made in the Midlands since acquisition.

##### **Customer Panel and Stakeholder Workshops**

The WPD Customer Panel was introduced in 2011. The panel meets four times a year and members, who represent a wide range of customers and key stakeholder groups, help us keep up to speed with the issues affecting our customers. Through the Panel, WPD proactively seek honest and challenging customer views about the way we operate and our future plans. It has played an important role going forward in helping WPD develop its business plans and outputs for the next RIIO price control.

In November 2012 and February 2013 WPD held a series of stakeholder workshops in Exeter, Cardiff, Bristol, Nottingham, Birmingham and Gloucester to discuss options for the draft business plan for 2015-2023. The workshops focussed on the most important themes for our business plan, specifically in relation to the reliability of our network, customer service, innovation and the environment. The events were attended by over 200 people in total from stakeholders including large customers, suppliers, manufacturers, local authorities, emergency planners, environmental groups, students, vulnerable customer groups, parish councils, health trusts and universities. This included sessions specifically addressing social obligations and the views of future customers.

##### **Deaf Awareness Chartermark**

WPD holds the Action on Hearing Loss (formerly RNID) 'Louder Than Words' accreditation. We are the only DNO groups to have held the accreditation for 3 and 5 years respectively for WPD South Wales/WPD South West and WPD Midlands.

#### ***Future Networks - Research, Innovation and Low Carbon Networks***

As part of DPC5, Ofgem introduced the Low Carbon Network ("LCN") fund. It was set up to encourage DNOs to test new technology and commercial arrangements to support the UK's low carbon transition and climate change objectives.

The LCN fund, totalling £500m over the period 2010-2015, is made available through an annual Ofgem led competition for "flagship" demonstration projects (termed "Tier 2" projects). There is also an annual allowance allocated to each DNO (called "Tier 1" with £21m over the five years for WPD) to enable smaller demonstration projects to be developed with less regulatory oversight. WPD also has an active research and development programme focussed on emerging technologies. This is supported by Ofgem's Innovation Funding Incentive ("IFI") scheme (with an allowance of up to £28m over the five years for WPD).



## **Directors' report (continued)**

For the year ended 31 March 2013

### **Business review (continued)**

#### ***Future Networks - Research, Innovation and Low Carbon Networks (continued)***

After three years of operation WPD has secured funding for five Tier 2 flagship projects, worth approximately £50m, more than any other DNO group, making WPD a clear leader in network innovation. The projects are making good progress with valuable learning emerging as we try new solutions.

- 2011 – LV Templates for a Low Carbon Future – Based on LV data collected from the most extensively monitored distributed network in Britain (nearly 1,000 substations in South Wales). The project is in the final stages of developing a new suite of customer consumption profiles that will enable us to improve our utilisation of network assets without impacting customer supply security.
- 2011 – The Lincolnshire Low Carbon Hub – The project is building a 33kV renewable generation ready “hub” across a large part of the East Midlands coastal region. After several technical network design challenges and a shift in government policy towards onshore wind, the project has now moved into the construction stage. The project timeline will be recovered during the construction stage.
- 2012 – Flexible and Low Carbon Optimised Networks (“FALCON”) – The project is developing a fully interactive 11kV power flow nodal model for the city of Milton Keynes. The model (called a “SIM” – Scenario Investment Model) will be populated by data on the real time state of the local grid, together with feedback from a suite of smarter grid demonstration techniques across the city. It will allow DNOs to automatically develop optimised investment plans based on a range of future energy scenarios.
- 2012 – SoLa BRISTOL – The project is demonstrating the concept of coordinating disparate energy controllers located at customer premises, to maintain substations within capacity. The project will provide valuable control logic for future despatch and control of virtual power plants and electric vehicle charging. In this project the remote energy is stored in battery systems, charged from PV (photovoltaic solar panel) systems on customer roofs. The project also includes the conversion of some customer internal system from alternating to direct current (AC to DC) to improve energy efficiency.
- 2013 – FlexDGrid – The transition of the UK energy system from one of centralised energy generation, to one where distributed generation plays a greater role, is leading to new network challenges. In particular the introduction of CHP (combined heat and power) in urban environments is leading to a significant increase in electrical short circuit potential currents (called the “Fault Level”). This new project will demonstrate innovative means of modelling, measuring and controlling fault levels in 10 primary substations serving the central business district of Birmingham, Britain’s second largest city.

WPD have also registered eleven Tier 1 projects with Ofgem covering a broad range of topics, including such themes as wireless charging of electric vehicles and supporting community based energy initiatives. The research and development programme consists of approximately 30 projects, in addition to several national programmes where WPD collaborates with other industry organisations.

In autumn 2012 WPD hosted the national Low Carbon Networks annual conference. The event, held in the Millennium Centre Cardiff, was a huge success, receiving praise from Ofgem and UK government attendees. It was attended by over 500 delegates, double the number in the previous year. Delegates represented energy businesses from across Europe, UK academia and global manufacturers.

## **Directors' report (continued)**

For the year ended 31 March 2013

### **Business review (continued)**

#### ***Social and community issues***

##### **WPD Community Support/Sponsorship programme 2012/13**

WPD's Community Support Policy is reviewed annually by WPD's executive and endorsed by the Chief Executive Officer. We identify areas where business issues link to social issues, and determine criteria that all community support projects must meet. We work in partnership with local community groups to deliver a wide range of projects. The three themes of education, safety and the environment continue to form the bedrock of our support activity during a year that saw assistance to around 350 separate charitable and non-charitable organisations. Highlights included:

- continuing our tree planting partnerships with the British Trust for Conservation Volunteers and the Silvanus Trust (over 7,000 trees and shrubs planted), whilst our "Keen to be Green" brand has also been used to develop links with Wildlife Trusts in Derby, Leicestershire & Rutland, Gloucester, Avon, Somerset, Devon and parts of Wales, with Wildfowl and Wetland schemes, and as part of environmental awards involving a number of schools.
- continuing to promote WPD's Priority Services Register with roadshows and events involving organisations like Wales Council for the Blind, Age UK and Age Cymru, who we also enlisted to provide specialist training for WPD Contact Centre staff dealing with older customers
- working with the police and other agencies as part of anti-metal theft and safety initiatives. Cable information booklets and wall charts were produced to enable scrap dealers and police to easily identify WPD property, while new "Substation Watch" leaflets and fridge magnets were targeted at encouraging customers to report anything suspicious around our infrastructure
- our two community education safety advisers attended around 120 separate events during the year for schoolchildren, including school visits, crucial crew and lifeskills initiatives across all WPD regions
- launching WPD's new education website in September 2012, the Power Discovery Zone, an interactive, curriculum-linked resource for schools that relates to electricity and safety
- partnering three regional newspapers in a six month Cash for the Community initiative which began in October 2012 (covering West Wales, Devon and Gloucestershire). We provided funding of £25,000 per region to support community groups, charities and not-for-profit organisations.
- sponsoring a series of community pride awards across the Midlands at Northamptonshire, Loughborough and Stratford

While maintaining these three core themes, we have also continued to tailor our support to align, where appropriate, with the feedback from our stakeholder and customer opinion research. In particular, we have sought to establish initiatives, like our Community Chest partnership with the Centre for Sustainable Energy, that help 'fuel poor' customers reduce their energy consumption. An investment of £65,000 during the year provided grants to 66 successful applicants from across our network area for such things as heating and lighting upgrades, insulation and door and window draft excluders at community buildings and village halls run by trusts or non-profit making groups.

#### ***Capital investment***

Gross capital investment (before customers' contributions) during the period was £249.6m across the WPD West Midlands region and included the replacement of overhead lines and switchgear together with the introduction of new technology.

## **Directors' report (continued)**

For the year ended 31 March 2013

### **Business review (continued)**

#### ***Capital investment (continued)***

A number of significant projects were undertaken during the year.

- Boughton Road 132/11kV substation A number of ageing WPD assets in the East Birmingham area of the West Midlands were nearing the end of their useful life Two existing 33/11kV substations at Boughton Road and Este Road, both in the east of Birmingham, have been replaced with a new combined 132/11kV substation located at Boughton Road Two 132/11kV 60 MVA transformers and a 2 switch 132kV GIS cross bay have been installed to accommodate existing and future load growth Associated existing 33kV fluid filled cables are oil pressurised and have been subject to a number of leaks and have been decommissioned in conjunction with this project with associated environmental and network reliability improvements The 11kV load from Este Road substation has been transferred to a newly commissioned 35 panel 11kV switchboard at the new Boughton Road substation Project costs are circa £14m Work to completely decommission the existing Este Road site will continue into 2013
- Bishops Wood 275/132kV substation Bishops Wood is a 275/132kV grid supply point located in Worcestershire in the south of the West Midlands The site was commissioned in 1968 and is a double bus bar arrangement WPD own the 132kV bus bars and associated equipment The WPD-owned 132kV circuit breakers were GEC bulk oil type and over 44 years old Spares are difficult to obtain, and condition assessment showed they have come to the end of their useful life The Bishops Wood feeder protection is also now obsolete and at risk of failure This scheme has replaced 4 (WPD-owned) 132kV GEC bulk oil circuit breakers with modern Siemens SF6 equivalents along with associated protection and control panels, multicores, voltage transformers and associated support structures at a total cost of approximately £800,000

#### **Regulatory issues**

2012/13 was the third year of the five year DPC5 price control period WPD West Midlands will be allowed to increase its prices by an average of 4.3% plus inflation in each of the five years of DPC5.

In order to comply with the requirements of our licence and the Competition Act, WPD continued with its compliance programme to ensure that all our policies and procedures meet legal requirements As part of the programme, all WPD staff have received an updated code of conduct on fair competition.

During the eleventh full year of Ofgem's IIS, WPD West Midlands believes it has, at a minimum, met its regulatory targets for each of the three key areas to which the incentive scheme applies, namely

- the number of interruptions that customers experience,
- the duration of those interruptions, and
- the quality of telephone response from the distribution business to the customer.

The incentive scheme can lead to an increase or a reduction in revenue depending on performance Subject to confirmation of the declared year-end results by Ofgem's auditors, we have exceeded our targets for network performance and earned an income uplift for the year. We have been set annual targets by Ofgem for customer minutes lost and customer interruptions for the current price control period which runs until March 2015.

## **Directors' report (continued)**

For the year ended 31 March 2013

### **Principal risks and uncertainties**

#### *Regulatory risk*

The substantial part of the Company's revenue is regulated and is subject to a review every five years. The latest review became effective on 1 April 2010 and continues to 31 March 2015.

Under the review, Ofgem assesses the revenue and capital expenditure plans of the Company and determines what they consider an efficient level of that expenditure. Ofgem also considers the required cost of capital sufficient to encourage the required investment in the network, and determines customer service targets.

WPD's management invests considerable resources in the review process and has been proactive in working with Ofgem to establish better measures of cost recording to inform future reviews.

If the Company feels that, as a result of a review it would financially be unable to continue to operate and to meet its obligations under the licence, then it has the right to refer the matter to the Competition Commission for a determination.

The Company's regulated income and also the Regulatory Asset Value ("RAV") are to some extent linked to movements in the RPI. Reductions in the RPI would adversely impact revenues and the debt/RAV ratio.

#### *Network disruption*

Disruption to the network could reduce profitability both directly through the lower units delivered on which income is charged, and also through the system of penalties and rewards that Ofgem has in place relating to customer service levels (discussed under 'Network performance' above).

There are economic restrictions on the level of capital expenditure that can be incurred to make the network totally reliable. A certain level of risk must be accepted and this is recognised by Ofgem in its regulatory review. However, the Company believes that its network is robust. It targets capital expenditure on schemes which are assessed to have the greatest improvement in customer service levels. It also spends considerable sums on routine maintenance, including tree cutting to keep trees away from lines both for safety reasons and as trees have been proven to be a major cause of network interruptions. The Company has met Ofgem's targets for customer service.

#### *Reliance on suppliers*

WPD relies on a limited number of suppliers for cable laying and tree cutting services, and for the supply of cables, plant and machinery. However WPD considers that there are sufficient alternative suppliers such that, should an existing supplier be unable to continue to make supplies, then there will be no significant long-term impact on WPD's ability to operate the network.

Most of the electricity which enters WPD's network is carried on the national grid and enters WPD's network at a limited number of grid supply points. WPD is dependent on the national grid. However, this is also an activity regulated by Ofgem and thus the risk of a major failure is considered very remote.

#### *Environment*

There is always the risk that changes in legislation relating to environmental and other matters, including those imposed on the UK by the European Union, could result in considerable costs being incurred by the Company with no guarantee that Ofgem would allow them to be recovered through regulated income.

## **Directors' report (continued)**

For the year ended 31 March 2013

### **Principal risks and uncertainties (continued)**

#### *Creditworthiness of customers*

Most of WPD's income is for the delivery of electricity to end-users and thus its customers are the suppliers to those end-users. It is a requirement that all licensed electricity distributors and suppliers become parties to the Distribution Connection and Use of System Agreement. This agreement sets out how creditworthiness will be determined and, as a result, whether the supplier needs to provide collateral. The risk of a significant bad debt is thus considered low.

#### *Pensions*

Most employees are members of a defined benefit pension scheme, which also has a considerable number of members who are either retired or have deferred benefits. There are risks associated with the financial performance of the assets within the scheme and with the estimate of the liabilities of the scheme including longevity of members. Currently, ongoing service costs and a proportion of the deficit costs are recoverable through regulated income.

The defined benefit pension schemes operated by WPD are, with very limited exception, closed to new members. A defined contribution scheme is offered to new employees instead. As time elapses, this will reduce WPD's exposure associated with defined benefit pension plans.

#### *Internal control environment*

The directors of WPD have overall responsibility for the system of internal controls and for reviewing the effectiveness of the system. The system of internal controls is designed to manage rather than eliminate the risk of failure to achieve business objectives. In pursuing these objectives, internal control can only provide reasonable and not absolute assurance against material mis-statement or loss.

There are many cultural features in WPD that contribute directly to the success of WPD and the results that it has achieved. These include:

- good definition and communication of short-term business objectives and targets
- commitment to achievement of objectives and targets.
- speedy decision-making
- business environment that empowers managers
- an uncomplicated management structure that aids the flow of information both ways through the organisation

In order for this success to occur, the control environment is one which empowers those with direct responsibility to take decisions within a clearly defined control framework. The control mechanisms have to be sufficient to limit risk but appropriate to the Company's ability to react quickly and effectively to events, therefore enabling the Company to deliver results over a sustained period of time.

It is important for an organisation to have a clearly defined structure of control expectations. The controls start at director level and make it clear to everyone concerned how the business should be conducted (policy) and how far each person can go in conducting that business (authority levels). This information is communicated effectively to all levels of staff.

As WPD is owned by a US publicly quoted company, it is subject to the requirements of the US Sarbanes-Oxley Act of 2002. As permitted by the Act, the application of Sarbanes-Oxley was not applied to WPD Midlands until 1 December 2011 when the WW Group's financial processes were implemented across WPD Midlands. From this time, the same controls as apply in the WW Group have also applied to WPD Midlands.

## **Directors' report (continued)**

For the year ended 31 March 2013

### **Principal risks and uncertainties (continued)**

#### *Internal control environment (continued)*

There are two main components of the Act, SOX302 and SOX404

Under Section 302 of this Act, senior managers affirm quarterly that disclosure controls have been evaluated and are operating effectively, that there are no material internal control issues or, if there are, that they have been reported to PPL's Audit Committee

Section 404 is an annual process which includes the evaluation of internal controls for financial reporting WPD comply with these requirements via a two stage approach

Firstly, Company level controls which are pervasive across the Company are documented and tested The controls cover the COSO elements of effective internal control which encompass:

- control environment
- risk assessment
- information and communication
- control activities
- monitoring

Secondly, all the major financial processes have been documented with specific detail on the controls in place This includes the Information Technology environment which supports the financial processes Management monitor and test these controls on an ongoing basis In addition, the controls are reviewed by the Internal Audit department and any issues identified are communicated back to management and the process owners to enable improvement to the controls

Annually, WPD's compliance with the Act is also reviewed in detail by WPD's external auditors Good controls together with appropriate documentation must be maintained, and this is subject to testing by management and both internal and external auditors on an annual basis Since inception of the Act, no significant deficiencies nor material weaknesses have been identified in WPD's financial control environment

#### *Treasury*

##### Risk management

WPD does not undertake transactions in financial derivative instruments for speculative purposes.

All items in WPD West Midlands are denominated in sterling and therefore there is no currency risk exposure

##### Credit rate risk

WPD West Midlands, WPD East Midlands, WPD South Wales and WPD South West are required by their distribution licences to maintain investment grade ratings, which they have done WPD West Midlands has the following long-term corporate credit ratings Moody's Baa1 and Standard & Poor's BBB.

Any cash deposits are only made to third parties with a high credit rating (not below a long-term rating of A/A2/A and a short-term rating of A1/P1/F1 by Standard and Poor's, Moody's and Fitch, respectively) and within strict limits imposed by the appropriate Board

## **Directors' report (continued)**

For the year ended 31 March 2013

### **Principal risks and uncertainties (continued)**

#### *Treasury (continued)*

##### Interest rate risk

Substantially all of the Company's external debt is long term and at fixed rates of interest

##### Liquidity and going concern

On a day-to-day basis, WPD South West provides liquidity to the whole of WPD. It has borrowing arrangements in place with a range of third parties with high credit ratings. At 31 March 2013, WPD South West had committed borrowing facilities available in respect of which all conditions precedent had been met at that date of £245.0m maturing January 2017 all of which was undrawn at 31 March 2013. In addition, it had uncommitted facilities of £65.0m all of which was undrawn at 31 March 2013.

At 31 March 2013, WPD West Midlands had committed borrowing facilities available, in respect of which all conditions precedent had been met at that date, of £300.0m maturing April 2016. Under this facility WPD West Midlands has the ability to request the lenders to issue up to £80.0m of letters of credit in lieu of borrowing. At 31 March 2013, £6.0m had been borrowed against the facility and no letters of credit issued. In addition, it had uncommitted facilities of £2.5m all of which was undrawn at 31 March 2013.

At 31 March 2013, WPD West Midlands had £1,039.8m (2012: £1,032.9m) of external debt outstanding of which £6.0m (2012: £0.1m) was short term. It had cash and short term deposits of £0.7m (2012: £80.0m).

After consideration, the directors of the Company have concluded that the Company has sufficient resources available to enable it to continue in existence for the foreseeable future and at least for a period of 12 months from the date of signing the accounts and have therefore continued to adopt the going concern basis in preparing the financial statements. This consideration included the availability of facilities as set out above, the relatively stable and regulated nature of the business, the forecast long term business plan, and the anticipated ability of the Company to be able to raise additional long term debt in the future.

### **Results and dividends**

The profit for the 12 months to 31 March 2013 is £166.6m (15 months to 31 March 2012: £40.4m). Profit on ordinary activities before tax is £207.4m (15 months to 31 March 2012: £73.1m). For the 15 months to 31 March 2012, there were exceptional charges of £143.7m before tax.

For the year to 31 March 2013, dividends paid by the Company totalled £77.2m (15 months to 31 March 2012: £982.0m).

### **Payment of creditors**

WPD's policy in respect of its suppliers (other than those providing electricity utility supplies and services) is to require suppliers to accept our terms which are displayed on our official orders unless alternative terms of mutual benefit can be agreed. The average length of time for the payment of creditors during the year to 31 March 2013 was 21 days (12 months to 31 March 2012: 16 days).

## Directors' report (continued)

For the year ended 31 March 2013

### Charitable donations

During the year ended 31 March 2013, donations of £68,377 were made by the Company to community organisations of which £9,133 was donated to charities. In addition, the WW Group has established a charitable foundation with donations of £2.0m, the foundation made donations of £19,180 to organisations in the WPD West Midlands area in 2012/13.

### Political donations and expenditure

WPD is a politically neutral organisation and, during the year, made no political donations.

### Equal opportunities

WPD is committed to equality of opportunity in employment and this is reflected in its equal opportunities policy and employment practices. Employees are selected, treated, and promoted according to their abilities and merits and to the requirements of the job. Applications for employment by people with disabilities are fully considered, and in the event of members of staff becoming disabled, every effort is made to ensure that their employment with WPD continues by way of making adjustments to their role and/or working environment or through retraining arranged as appropriate. It is the policy of WPD that the training, career development and promotion of disabled persons should, as far as possible, be identical to that of other employees.

### Employee consultation

WPD places considerable value on the involvement of its employees in its affairs. Staff are kept informed of WPD's aims, objectives, performance and plans, and their effect on them as employees through newsletters, regular team briefings and other meetings, as well as through WPD's in-house journal. Formal meetings are held regularly between senior managers and representatives of staff and their unions to discuss matters of common interest. A series of road show presentations by the directors each year ensure that all staff are aware of, and can contribute to, WPD's corporate goals.

### Directors and their interests

The directors who served during the year were as follows

	<u>Appointed</u>
RA Symons, Chief Executive	1 April 2011
DG Harris, Resources and External Affairs Director	1 April 2011
DCS Oosthuizen, Finance Director	1 April 2011
RL Klingensmith, non-executive director and President PPL Global	1 April 2011
ME Fletcher, independent director	31 October 2011

During and at the end of the financial period, no director was materially interested in any contract of significance in relation to the Company's business other than service contracts.

Insurance in respect of directors and officers is maintained by WPD's parent, PPL Corporation. The insurance is subject to the conditions set out in the Companies Acts and remains in force at the date of signing the Directors' report.

Subsequent to the year end, on 18 June 2013 the Board approved the appointment of P Swift as a Director with effect from 1 July 2013. He will be Operations Director.

### Regulatory financial statements

As a condition of its Electricity Distribution Licence, the Company is required to prepare and publish separate financial statements for its distribution business for each year ending 31 March. The Company will publish information on its website and this information will also be available from the Company's registered office as shown below.



## **Directors' report (continued)**

For the year ended 31 March 2013

### **Statement of disclosure to auditors**

So far as each person who was a director at the date of approving this report is aware, there is no relevant audit information, being information needed by the auditor in connection with preparing its report, of which the auditor is unaware. Having made enquiries of fellow directors and the Company's auditor, each director has taken all the steps that he is obliged to take 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.

### **Responsibility statements under the Disclosure and Transparency Rules**

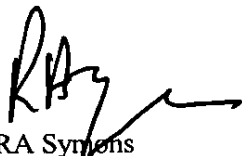
Each of the directors listed above confirm to the best of their knowledge

- (a) the financial statements, prepared in accordance with UK Generally Accepted Accounting Practice, give a true and fair view of the assets, liabilities, financial position and profit of the Company; and
- (b) the Directors' report includes a fair review of the development and performance of the business and the position of the Company together with a description of the principal risks and uncertainties that it faces

### **Auditors**

Ernst & Young LLP have expressed their willingness to continue in office and a resolution proposing their re-appointment will be put before the Annual General Meeting.

By Order of the Board



RA Symons  
Chief Executive

10 July 2013

**Western Power Distribution (West Midlands) plc**

Avonbank

Feeder Road

Bristol BS2 0TB

## Statement of directors' responsibilities

The directors are responsible for preparing the Directors' report and the financial statements in accordance with applicable law and regulations

Company law requires the directors to prepare financial statements for each financial period. 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 affairs of the Company and of the profit or loss of the Company for that period. 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 confirm that the financial statements comply with the above requirements

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

## **Independent auditors' report to the members of Western Power Distribution (West Midlands) plc**

We have audited the financial statements of Western Power Distribution (West Midlands) plc for the year ended 31 March 2013 which comprise the Profit and loss account, the Statement of total recognised gains and losses, the Balance sheet, the Statement of cash flows and Notes to the statement of cash flows A to C, and the related Notes 1 to 23. 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 auditors**

As explained more fully in the Statement of directors' responsibilities (set out on page 16), 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 March 2013 and of its profit for the period 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 period for which the financial statements are prepared is consistent with the financial statements.

## **Independent auditors' report**

**to the members of Western Power Distribution (West Midlands) plc (continued)**

### **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

*Ernst & Young LLP*

Christabel Cowling, Senior Statutory Auditor

*for and on behalf of Ernst & Young LLP, Statutory Auditors, Bristol*

15 July 2013

## Profit and loss account

For the year ended 31 March 2013

		For the 12 months ended 31 March 2013 £m	For the 15 months ended 31 March 2012		
	Note		Before exceptional items £m	Exceptional items £m	Total £m
<b>Turnover</b>	2	<b>436.0</b>	482.7	-	482.7
<b>Operating expenses</b>	3	<b>(166.9)</b>	(192.6)	(141.7)	(334.3)
<b>Operating profit/(loss)</b>	4	<b>269.1</b>	290.1	(141.7)	148.4
<b>Profit/(loss) on disposal of fixed asset</b>		<b>0.3</b>	(5.0)	-	(5.0)
<b>Profit/(loss) on ordinary activities before interest and tax</b>		<b>269.4</b>	285.1	(141.7)	143.4
Interest receivable and similar income	5	1.1	1.9	-	1.9
Interest payable and similar charges	5	(63.1)	(70.2)	(2.0)	(72.2)
<b>Profit/(loss) on ordinary activities before tax</b>	2	<b>207.4</b>	216.8	(143.7)	73.1
<b>Tax on profit/(loss) on ordinary activities</b>	6	<b>(40.8)</b>	(70.6)	37.9	(32.7)
<b>Profit/(loss) for the financial period</b>		<b>166.6</b>	146.2	(105.8)	40.4

All activities relate to continuing operations

There is no difference between the profit/(loss) on ordinary activities before tax and the profit/(loss) for the financial period stated above, and their historical cost equivalents

The accompanying notes are an integral part of these financial statements

# Statement of total recognised gains and losses

For the year ended 31 March 2013

		For the 12 months ended 31 March 2013 £m	For the 15 months ended 31 March 2012 £m
	Note		
Profit for the financial period		166.6	40.4
Movement on hedging reserve (net of tax)	19	(4.7)	(4.2)
<b>Total recognised gains for the period</b>		<b>161.9</b>	<b>36.2</b>
Prior period adjustment		-	(10.4)
<b>Total recognised gains since last annual report</b>		<b>161.9</b>	<b>25.8</b>

The accompanying notes are an integral part of these financial statements

**Balance sheet**

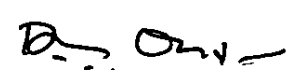
31 March 2013

	Note	2013 £m	2012 £m
<b>Fixed assets</b>			
Tangible assets	11	2,099.9	1,921.7
		<b>2,099.9</b>	<b>1,921.7</b>
<b>Current assets</b>			
Stocks	12	2.9	3.0
Debtors	13	200.0	189.9
Short-term deposits		-	70.0
Cash at bank		0.7	10.0
		<b>203.6</b>	<b>272.9</b>
<b>Creditors</b>			
Amounts falling due within one year	14	(178.1)	(163.8)
<b>Derivative financial instruments</b>			
Amounts falling due within one year	15	(6.3)	-
<b>Net current assets</b>		<b>19.2</b>	<b>109.1</b>
<b>Total assets less current liabilities</b>		<b>2,119.1</b>	<b>2,030.8</b>
<b>Creditors</b>			
Amounts falling due after more than one year	14	(1,033.8)	(1,032.8)
<b>Provisions for liabilities and charges</b>	16		
Deferred tax		(104.6)	(94.2)
Other		(28.5)	(36.3)
<b>Net assets</b>		<b>952.2</b>	<b>867.5</b>
<b>Capital and reserves</b>			
Called-up share capital	18	100.1	100.1
Share premium account	19	713.6	713.6
Hedging reserve	19	(8.9)	(4.2)
Profit and loss account	19	147.4	58.0
<b>Equity shareholders' funds</b>	20	<b>952.2</b>	<b>867.5</b>

The accompanying notes are an integral part of these financial statements

The financial statements on pages 19 to 44 were approved by the Board of Directors on 10 July 2013 and were signed on its behalf by

  
RA Symons  
Chief Executive

  
DCS Oosthuizen  
Finance Director

## Statement of cash flows

For the year ended 31 March 2013

		For the 12 months ended 31 March 2013	For the 15 months ended 31 March 2012
	Note	£m	£m
<b>Net cash inflow from operating activities</b>	A	<b>239.2</b>	<b>270.7</b>
<b>Returns on investments and servicing of finance</b>			
Interest received		1.1	1.8
Interest paid		(58.0)	(30.6)
Issue costs on new long-term loans		-	(0.8)
Payment on termination of interest rate swaps		-	(10.8)
Net cash outflow from returns on investments and servicing of finance		(56.9)	(40.4)
<b>Tax/group relief paid</b>		<b>(21.9)</b>	<b>(28.4)</b>
<b>Capital expenditure and financial investment</b>			
Purchase of tangible fixed assets		(259.5)	(302.9)
Customers' contributions received		29.0	54.4
Transfer of tangible fixed assets to other WPD undertakings		0.9	-
Sale of tangible fixed assets		0.4	-
Net cash outflow from capital expenditure and financial investment		(229.2)	(248.5)
<b>Equity dividends paid</b>		<b>(77.2)</b>	<b>(982.0)</b>
<b>Cash outflow before use of liquid resources and financing</b>		<b>(146.0)</b>	<b>(1,028.6)</b>
<b>Management of liquid resources</b>			
Decrease/(increase) in short-term deposits		70.0	(70.0)
Net cash inflow/(outflow) from management of liquid resources		70.0	(70.0)
<b>Financing</b>			
Issue of ordinary share capital		-	813.7
New long-term loans		-	785.6
Increase/(decrease) in balances due from other WPD undertakings		60.8	(490.8)
Increase in short term debt		5.9	0.1
Net cash inflow from financing		66.7	1,108.6
<b>(Decrease)/increase in cash in the period</b>	B, C	<b>(9.3)</b>	<b>10.0</b>

The accompanying notes are an integral part of these financial statements



## Notes to the statement of cash flows

For the year ended 31 March 2013

### A. Reconciliation of operating profit to net cash inflow from operating activities

	12 months ended 31 March 2013 £m	15 months ended 31 March 2012 £m
Operating profit	269.1	148.4
Depreciation	48.1	55.3
Decrease in stocks	0.1	1.9
Increase in debtors	(69.2)	(22.1)
(Decrease)/increase in creditors	(1.0)	51.1
(Decrease)/increase in provisions	(7.9)	36.1
Net cash inflow from operating activities	239.2	270.7

### B. Reconciliation of movement in net debt

	At 1 April 2012 £m	Cash Flow £m	Other non-cash changes £m	At 31 March 2013 £m
Cash at bank	10.0	(9.3)	-	0.7
Short-term deposits	70.0	(70.0)	-	-
Debt due within one year				
Bank loans and overdrafts	(0.1)	(5.9)	-	(6.0)
Debt due after one year				
£250m 6.0% sterling bond 2025	(246.6)	0.2	(0.3)	(246.7)
£800m 5.75% bonds 2032	(786.2)	(0.2)	(0.7)	(787.1)
Increase in external borrowings (Note C)		(5.9)		
Balances with other WPD undertakings	107.9	(60.8)	0.1	47.2
	(845.0)	(146.0)	(0.9)	(991.9)

Other non-cash changes (other than balances with other WPD undertakings) relate to the amortisation of bond issue costs

## Notes to the statement of cash flows

For the year ended 31 March 2013

### C. Reconciliation of net cash flow to movement in net debt

	12 months ended 31 March 2013 £m	15 months ended 31 March 2012 £m
(Decrease)/increase in cash in the period	(9.3)	10.0
(Decrease)/increase in short-term deposits	(70.0)	70.0
Increase in external borrowings	(5.9)	(785.7)
Change in balances with other WPD undertakings	(60.8)	490.8
Increase in net debt resulting from cash flows	(146.0)	(214.9)
Non-cash changes	(0.9)	(0.6)
Increase in net debt in period	(146.9)	(215.5)
Net debt at start of period	(845.0)	(629.5)
Net debt at end of period	(991.9)	(845.0)

## **Notes to the financial statements**

For the year ended 31 March 2013

### **1. Accounting policies**

The principal accounting policies are summarised below

#### **Basis of preparation**

The financial statements have been prepared on the going concern basis under the historical cost convention and in accordance with the Companies Act 2006 and applicable accounting standards. Accounting policies are prepared under United Kingdom Generally Accepted Accounting Practice ("UK GAAP"). They have been applied consistently throughout the year and the preceding period.

In the prior period the Company decided to align the year end for statutory account purposes with that for regulatory purposes as they both follow a similar format. Thus the previous financial period was for 15 months to 31 March 2012.

Therefore the results for the year ended 31 March 2013 are compared with the 15 month period to 31 March 2012 and represent accounting periods of different lengths.

As permitted by FRS 29 "Financial Instruments: Disclosure", full disclosure relating to financial instruments is consolidated with those of the PPL WEM Holdings plc group and is incorporated in the disclosure in the WEM Group financial statements.

#### **Going concern**

The directors have prepared the financial statements on a going concern basis as they have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future due to the strength of its balance sheet. This is discussed further under 'Principal risks and uncertainties - treasury' within the Directors' report.

#### **Turnover**

Turnover is recognised to the extent that it is probable that economic benefits will flow to the Company and that the turnover can be reliably measured. Turnover comprises primarily use of energy system income. Turnover includes an assessment of the volume of unbilled energy distributed to customers between the date of the last meter reading and the period end. Remaining sales relate to the invoice value of other goods and services provided which also relate to the electricity network.

Where turnover received or receivable exceeds the maximum amount permitted by regulatory agreement and adjustments will be made to future prices to reflect this over-recovery, no liability is recognised as such an adjustment to future prices relates to the provision of future services. Similarly no asset is recognised where a regulatory agreement permits adjustments to be made to future prices in respect of an under-recovery.

#### **Leases**

Rentals for operating leases are charged to the profit and loss account in equal annual amounts over the period of the lease.

#### **Research**

Expenditure on research is written off to the profit and loss account in the period in which it is incurred.

## Notes to the financial statements

For the year ended 31 March 2013

### 1. Accounting policies (continued)

#### Share based payments

WPD operates a cash-settled phantom share option scheme for executive directors and senior managers. The cost of cash-settled transactions is measured at fair value using an appropriate option pricing model. Fair value is established at each balance sheet date from grant date until the awards are settled. During the vesting period a liability is recognised representing the product of the fair value of the award and the portion of the vesting period expired as at the balance sheet date. From the end of the vesting period until settlement, the liability represents the full fair value of the award as at the balance sheet date. Changes in the carrying amount of the liability are recognised in profit or loss for the period.

#### Pension costs

The Company participates in one defined benefit pension scheme, the Electricity Supply Pension Scheme ("ESPS"), to which most employees in the WEM Group belong. Under the guidance of Financial Reporting Standard ("FRS") 17 "Retirement Benefits", where an entity cannot separate out its share of the scheme's assets and liabilities on a reasonable and consistent basis, the relevant entity should account for pensions as if the scheme were a defined contribution scheme. Therefore the Company charges contributions to the profit and loss account and capital expenditure as they become payable in accordance with the rules of the scheme.

Any cost of ex gratia and supplementary pensions, including early retirement deficiency contributions, are charged to the profit and loss account when a detailed plan is formulated and communicated.

#### Interest costs

Interest charges are recognised in the profit and loss account as they accrue, on an effective rate basis.

#### Tangible fixed assets

Tangible fixed assets are stated at cost net of customer contributions, less amounts provided to write off the cost less anticipated residual value of the assets over their useful economic lives, which are as follows:

	Years
Distribution network assets	
Overhead lines and poles	45
Underground cables	70
Plant and machinery (transformers and switchgear)	45
Meters	Up to 10
Customer contributions	55
Other (towers and substation buildings)	Up to 55
Buildings - freehold	Up to 60
Fixtures and equipment	Up to 20
Vehicles and mobile plant	Up to 10

Freehold land is not depreciated.

The cost of self-constructed assets includes the cost of materials, direct labour and an appropriate proportion of production overheads, but excludes financing costs.

Significant IT consultancy and software development costs are capitalised when tangible benefits accrue and are amortised over their estimated useful economic life from the date of first use. Costs primarily relate to external suppliers, directly attributable internal costs are capitalised only if significant. Other IT consultancy and development costs are charged to the profit and loss account in the period in which they are incurred.

## **Notes to the financial statements**

For the year ended 31 March 2013

### **1. Accounting policies (continued)**

#### **Tangible fixed assets (continued)**

Assets are depreciated on a straight line basis. Customers' contributions towards distribution network assets, which include low carbon network funding and capital grants, are credited to the profit and loss account over the estimated useful lives of the related assets. The unamortised amount of such contributions is shown as a deduction from fixed assets. This is a departure from the Companies Act 2006 requirements which require fixed assets to be included at their purchase price or production cost and hence the unamortised amount of contributions 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 unamortised contributions is shown in Note 11.

The carrying values of tangible fixed assets are reviewed for impairment if events or changes in circumstances indicate the carrying value may not be recoverable.

#### **Stocks**

Stocks are valued at the lower of cost and net realisable value which takes account of any provision necessary to recognise damage and obsolescence.

#### **Short-term deposits**

Short-term deposits comprises deposits that do not qualify as cash at bank.

#### **Cash at bank**

Cash at bank comprises cash 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 assets**

Financial assets comprise loans and receivables and include trade receivables, other receivables, loans, and other investments. Financial assets are recognised initially at fair value, normally being transaction price. Financial assets are derecognised on sale or settlement.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are carried at amortised cost using the effective interest method if the time value of money is significant. Gains and losses are recognised in income when the loans and receivables are derecognised or impaired, as well as through the amortisation process. This category of financial assets includes trade and other receivables.

If there is objective evidence that an impairment loss on loans and receivables carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced, with the amount of the loss recognised in the profit and loss account.

## Notes to the financial statements

For the year ended 31 March 2013

### 1. Accounting policies (continued)

#### Financial liabilities

Financial liabilities include trade and other payables, accruals, and finance debt. These are initially recognised at fair value. For interest-bearing loans and borrowings, this is the fair value of the proceeds received net of issue costs associated with the borrowing. After initial recognition, financial liabilities are subsequently measured at amortised cost using the effective interest method. Amortised cost is calculated by taking into account any issue costs, and any discount or premium on settlement. Gains and losses arising on the repurchase, settlement or cancellation of liabilities are recognised respectively in interest and other revenues and finance costs.

#### Derivative financial instruments

WPD West Midlands uses derivative financial instruments such as forward interest rate swaps to hedge its risks associated with interest rate fluctuations. Derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

Losses relating to the effective portion in relation to forward interest rate swaps terminated prior to a previous debt issuance, that are deferred in the hedging reserve, are being recycled to the profit and loss account over the term of the bond. These swaps were designated as cash flow hedges, where they hedge the exposure to variability in cash flows that is attributable to a particular risk associated with a recognised asset, liability or forecasted transaction.

#### 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 will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. The estimate is discounted to present value where the effect is material.

#### Taxation

Current 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 tax in the future or a right to pay less tax in the future have occurred at the balance sheet date. Timing differences are differences between the Company's taxable profits and its results as stated in the financial statements that arise from the inclusion of gains and losses in tax assessments in years different from those in which they are recognised in the financial statements.

A net deferred tax asset is regarded as recoverable and therefore recognised only when, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted. Deferred tax is not recognised when fixed assets are sold and it is more likely than not that the taxable gain will be rolled over, being charged to tax only if and when the replacement assets are sold.

## Notes to the financial statements

For the year ended 31 March 2013

### 1. Accounting policies (continued)

#### Taxation (continued)

Deferred tax is measured at the average tax rates that are expected to apply in the years in which the timing differences are expected to reverse, based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date. Deferred tax is measured on a discounted basis to reflect the time value of money over the period between the balance sheet date and the dates on which it is estimated that the underlying timing differences will reverse. The discount rates used reflect the post-tax yields to maturity that can be obtained on government bonds with similar maturity dates and currencies to those of the deferred tax assets or liabilities.

### 2. Segmental reporting

Substantially all of the Company's turnover and profit before tax are derived from the delivery of electricity across its distribution network in the United Kingdom and related activities.

### 3. Operating expenses

The directors consider that the nature of the business is such that the analysis of expenses shown below is more informative than that set out in the formats specified by the Companies Act 2006.

	12 months ended 31 March 2013 £m	15 months ended 31 March 2012 £m
Employee costs (Note 8)	36.1	62.3
Depreciation	48.1	55.3
Property taxes	25.8	30.0
Other operating expenses	56.9	45.0
Operating expenses before exceptional costs	166.9	192.6
Exceptional costs comprise	12 months ended 31 March 2013 £m	15 months ended 31 March 2012 £m
Pension deficit payment associated with the acquisition	-	50.0
Severance costs	-	23.1
Pension costs associated with severance	-	18.9
Provision for bringing network maintenance up to required levels	-	26.9
Provision for cost of required network change	-	10.7
Costs associated with terminating contracts	-	3.3
Provision for unfunded pension liabilities	-	0.9
Accelerated depreciation on IT software	-	0.6
Other	-	7.3
Exceptional costs within operating expenses	-	141.7

Prior year exceptional interest cost is shown in Note 5. The tax rate on the above exceptional items has been credited at the effective rate shown in Note 6.

## Notes to the financial statements

For the year ended 31 March 2013

<b>4. Operating profit</b>	<b>12 months ended 31 March 2013 £m</b>	<b>15 months ended 31 March 2012 £m</b>
Operating profit is stated after charging		
Depreciation *	48.1	55.3
Operating lease rentals		
Plant, machinery and equipment	6.3	6.8
Land and buildings	1.6	0.9
Research and development **	0.1	-
Auditors' remuneration:		
Fees payable to the Company's auditors for the audit of the Company's annual accounts	0.2	0.2

\* Depreciation of fixed assets is stated net of depreciation capitalised of £6.2m (2012 £3.8m) in respect of equipment consumed during the construction of the electricity network

\*\* Research and development costs above exclude expenditure on Low Carbon Network projects which is capitalised together with associated funding received

<b>5. Interest</b>	<b>12 months ended 31 March 2013 £m</b>	<b>15 months ended 31 March 2012 £m</b>
Interest payable and similar charges		
On bank loans and overdrafts	0.9	2.9
On loans from other WPD undertakings	0.1	-
On loans from E.ON UK plc group companies	-	2.6
Other loans	62.1	64.7
	63.1	70.2
Interest receivable and similar income		
On loans to other WPD undertakings	(1.0)	(1.7)
Other	(0.1)	(0.2)
	(1.1)	(1.9)
Interest expense (net)	62.0	68.3

During the 15 months to 31 March 2012, in addition to the above an exceptional interest charge of £5.1m was incurred in relation to the ineffective element of the interest rate derivative entered into in anticipation of the issue of long-term debt during the period and an interest related creditor of £3.1m was written off



## Notes to the financial statements

For the year ended 31 March 2013

### 6. Tax on profit on ordinary activities

	12 months ended 31 March 2013 £m	15 months ended 31 March 2012 £m
(a) Analysis of charge in the period		
Current tax		
UK corporation tax on profits for the period	21.6	12.6
Adjustment in respect of prior years	7.4	0.1
Total current tax (Note 6(b))	29.0	12.7
Deferred tax		
Origination and reversal of timing differences	28.0	6.3
Decrease in discount	3.1	38.7
Impact of change in corporation tax rate	(9.0)	(24.6)
Adjustment in respect of prior years	(10.3)	(0.4)
Total deferred tax (Note 17)	11.8	20.0
Tax charge on profit on ordinary activities including exceptional items	40.8	32.7

## Notes to the financial statements

For the year ended 31 March 2013

### 6. Tax on profit on ordinary activities (continued)

#### (b) Factors affecting the current tax charge for the period

The current tax assessed for the period is different to the standard rate of corporation tax in the UK of 24% (2012 26 39%) The differences are explained below

	12 months ended 31 March 2013 £m	15 months ended 31 March 2012 £m
Profit on ordinary activities including exceptional items before tax	207.4	73 1
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK of 24% (2012 26 39%)	49.8	19 3
Effects of:		
Expenses not deductible and income not taxable for tax purposes	(0.2)	(0 4)
Timing difference between capital allowances and depreciation	(6.9)	(11.7)
Timing difference related to pensions	(19.2)	-
Other timing differences	(7.4)	(10.7)
Chargeable gain on sale of supply business *	5.5	16 1
Adjustments to tax charge in respect of prior years	7.4	0 1
Current tax charge for the year (Note 6(a))	29.0	12 7

\* Relates to a sale in a prior period

#### (c) Factors that may affect future tax charges

A change from 24% to 23% with effect from 1 April 2013 was enacted by the Finance Act 2012

Further reductions to 21% from 1 April 2014 and to 20% from 1 April 2015 have been announced but not substantively enacted at the balance sheet date and therefore are not included in these financial statements The impact of the expected reduction in tax rates to 20% is expected to reduce the undiscounted deferred tax liability provided at 31 March 2013 by approximately £27 2m in 2014 with a corresponding credit to the profit and loss account

## Notes to the financial statements

For the year ended 31 March 2013

### 7. Dividends

	12 months ended 31 March 2013 £m	15 months ended 31 March 2012 £m
Dividends on equity shares		
Interim dividends - 77.2 pence per share (2012 981.5 pence)	77.2	982.0

### 8. Employee costs and numbers (including executive directors)

	12 months ended 31 March 2013 £m	15 months ended 31 March 2012 £m
(a) Employee costs		
Total employee costs during the period amounted to		
Wages and salaries	81.0	84.0
Severance costs	0.2	23.1
Social security costs	8.5	8.8
Pension costs	15.5	18.7
Pension costs associated with severance	1.1	18.9
Total employee costs	106.3	153.5
Less allocated to capital expenditure	(70.2)	(49.2)
Charged to the profit and loss account	36.1	104.3

#### (b) Number of employees

The average number of employees in the year was 1,803 (4 months to 31 March 2012, following reorganisation to align with the WW Group, was 1,798). All employees work for the network distribution activity. This includes a proportion of WW Group staff who work in part for WPD West Midlands and excludes a proportion of WPD West Midlands staff who work in part for other WPD DNOs. In the 11 months to 30 November 2011 the average number of employees was 1,571. The increase includes employees who were previously employed by E.ON UK plc or by the Company's contractors.

#### (c) Share based payments

WPD issues to directors and senior employees share appreciation rights ("SARs") relating to the shares of WPD's ultimate parent, PPL Corporation. The SARs require WPD to pay the intrinsic value of the SAR to the director or employee at the date of exercise. WPD has recorded liabilities of £1.4m (2012: £1.1m). Fair value of the SARs is determined by using the Black-Scholes option-pricing model using the assumptions noted below. In 2013, WPD recorded total charges of £0.8m (2012: £0.7m) allocated roughly equally between WPD South West, WPD South Wales, WPD East Midlands and WPD West Midlands. The total intrinsic value at 31 March 2013 was £1.4m (2012: £0.5m).

## Notes to the financial statements

For the year ended 31 March 2013

### 8. Employee costs and numbers (including executive directors) (continued)

#### (c) Share based payments (continued)

The weighted average fair value of options granted during the regulatory year was £0.58 (2012 £0.26). The range of exercise prices for options outstanding at the end of the period was £24.14 - £11.97 (2012 £24.14 - £10.21)

The following table illustrates the number and weighted average exercise prices ("WAEP") of, and movements in, share options during the year

	2013 No.	2013 WAEP	2012 No.	2012 WAEP
Outstanding as at 1 April	1,016,479	18.41	696,463	18.68
Granted during the year	317,825	19.66	322,534	17.77
Exercised	(166,465)	16.31	(806)	11.49
Forfeited	(220)	17.32	-	-
Expired during the year	(2,852)	18.40	(1,712)	11.63
Outstanding at 31 March	1,164,767	19.05	1,016,479	18.41
Exercisable at 31 March	570,996	19.58	677,271	19.02
The inputs into the Black-Scholes option-pricing model were	31 March 2013		31 March 2012	
Expected volatility	18.50%		20.60%	
Expected life (years)	6		6	
Risk-free rate	0.750%		0.88%	
Expected dividend yield	5.46%		5.00%	

The risk-free interest rate reflects the yield for a US Treasury Strip available on the date of grant with constant rate maturity approximating the option's expected life. Expected life is calculated based on historical exercise behaviour. Volatility over the expected term of the options is evaluated with consideration given to prior periods that may need to be excluded based on events not likely to recur that had impacted PPL's volatility in those prior periods. Management's expectations for future volatility, considering potential changes to PPL's business model and other economic conditions, are also reviewed in addition to the historical data to determine the final volatility assumption. The dividend yield is based on several factors, including PPL's most recent dividend payment, as of the grant date and the forecasted stock price through 2013.

## Notes to the financial statements

For the year ended 31 March 2013

### 9. Pension commitments

#### Electricity Supply Pension Scheme ("ESPS")

The ESPS provides pension and other related defined benefits based on final pensionable pay to employees throughout the electricity industry. One segment of the ESPS (the Central Networks Group segment) relates to the WEM Group as a whole and most employees of the WEM Group are members of the ESPS. The assets are held in a trustee administered fund.

The WEM Group segment of the ESPS is closed to new members except in very limited circumstances, existing members are unaffected. A defined contribution scheme is offered to new employees.

Under the guidance of FRS 17, where an entity cannot separate out its share of the scheme's assets and liabilities on a reasonable and consistent basis, the relevant entity should account for pensions as if the scheme were a defined contribution scheme. Therefore the Company charges contributions to the profit and loss account and capital expenditure as they become payable in accordance with the rules of the scheme. Full FRS 17 disclosure for the ESPS is made in the consolidated financial statements of PPL WEM Holdings plc. A summary however follows. Comparative information prior to 1 April 2011 cannot be given as members were part of a larger E.ON UK plc segment of the ESPS prior to acquisition.

The financial assumptions used in calculating the figures for ESPS under FRS 17 in respect of the WEM Group were

	31 March 2013	31 March 2012
RPI inflation	3.00%	2.75%
CPI inflation	2.00%	2.00%
Rate of increase in salaries	4.25%	4.00%
Rate of increase to pensions in payment	2.90%	2.70%
Discount rate for scheme liabilities	4.06%	4.63%

The mortality assumptions are based on the recent actual mortality experience of members within the scheme and the assumptions also allow for future mortality improvements. The assumptions are that a member currently aged 60 will live on average for a further 26.3 years if they are male and for a further 28.9 years if they are female. For a member who retires in 2033 at age 60 the assumptions are that they will live on average for a further 28.5 years after retirement if they are male and for a further 29.7 years after retirement if they are female.

## Notes to the financial statements

For the year ended 31 March 2013

### 9. Pension commitments (continued)

#### Electricity Supply Pension Scheme ("ESPS")(continued)

The assets and liabilities of the ESPS for the WEM Group as a whole, at 31 March, were as follows

	31 March 2013 £m	31 March 2012 £m
Present value of obligations	2,846.4	2,493.7
Fair value of plan assets	(2,648.3)	(2,371.6)
Deficit in the scheme	198.1	122.1
Related deferred tax asset	(45.6)	(29.3)
Net pension liability	152.5	92.8

Employer contributions paid to the ESPS in respect of the WEM Group during the year were £171.1m (2012: £53.0m). Payments in the current year include a deficit contribution of £136.1m.

#### Other scheme

WPD also operates a defined contribution scheme. The assets of the scheme are held separately from those of WPD in an independent fund administered by the scheme trustee. The pension arrangement available to all new employees in WPD commenced with effect from 1 April 2010 and employees of the WEM Group who were not members of the ESPS could join from 1 April 2011. At 31 March 2013 there were 1,300 members (2012: 929). The market value of the assets of the open section of the scheme was £5.3m (2012: £1.0m). Employer contributions to the scheme amounted to £2.3m in the year (2012: £0.8m).

## Notes to the financial statements

For the year ended 31 March 2013

### 10. Directors' emoluments

#### Current directors

The service contracts for the executive directors are with WPD South West. However, their emoluments include those for services to both the PPL WW and PPL WEM Groups as a whole. The emoluments detail given in this note represents total emoluments of the directors for all services provided to WPD companies as a whole. The costs are apportioned between WPD South Wales, WPD South West, WPD West Midlands and WPD East Midlands.

#### Previous directors

The emoluments of the two executive directors were in respect to services to the Company and the affiliate WPD East Midlands (previously Central Networks East plc). The values shown below are their total emoluments, the costs were however apportioned between the two companies. Their costs for the prior period relate to the three months to 1 April 2011, when the Company was acquired and the directors resigned. The non executive directors received no emoluments from the Company during either period, their remuneration was borne by E.ON UK plc and not recharged.

	<u>Highest paid director</u>		<u>Total</u>	
	<u>12 months ended</u>	<u>15 months ended</u>	<u>12 months ended</u>	<u>15 months ended</u>
	<u>31 March</u>	<u>31 March</u>	<u>31 March</u>	<u>31 March</u>
	<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>
	<u>£000</u>	<u>£000</u>	<u>£000</u>	<u>£000</u>
<hr/>				
<u>Current directors</u>				
The emoluments of the executive directors comprised				
Base salary (note i)	720	486	1,316	1,059
Performance dependent bonus (note ii)	449	440	876	861
Integration bonus (note iii)	352	352	753	753
Long term incentive plan (note iv)	408	440	997	440
Pension compensation allowance (note v)	461	839	1,049	1,805
Fees to the independent non executive director (note vii)	-	-	30	12
 <u>Previous directors (viii &amp; ix)</u>				
<u>Aggregate emoluments</u>				
Base salary	-	104	-	151
Bonus	-	1,087	-	1,521
Compensation for loss of office	-	922	-	1,163
	<b>2,390</b>	<b>4,670</b>	<b>5,021</b>	<b>7,765</b>
<hr/>				

(i) Base salary also includes benefits in kind.

(ii) The amount of the annual bonus is currently based on the WW Group's financial performance, the reliability of the electricity network, customer satisfaction, and other factors.

(iii) The integration bonus is in respect of the WEM Group's financial performance within each of the two years shown above, which covers the period since acquisition.

## Notes to the financial statements

For the year ended 31 March 2013

### 10. Directors' emoluments (continued)

(iv) Under a long term incentive plan, the three current executive directors receive phantom stock options. The option price is set at the quoted share price of WPD's parent in the US, PPL Corporation, at the date the phantom options are granted. The options may be exercised during fixed periods and the gain is payable through the payroll. The values above include any payments made to the executive directors in respect of gains in value of phantom options exercised in the year. In 2013, three executive directors were granted options (2012: three) and three executive directors exercised options (2012: nil). In addition, WPD's Chief Executive Officer and, from 2013 WPD's Finance Director receive annually a grant of PPL Corporation shares which cannot generally be accessed for three years, a number of these shares is dependent on the achievement of certain criteria at PPL. The value of these shares is shown within this line.

(v) In anticipation of the change in tax applicable to UK pensions effective 6 April 2006, the executive directors resigned as active members of the WW Group's segment of the Electricity Supply Pension Scheme ("ESPS" - note 9) on 5 April 2006 and elected for enhanced protection. WPD thus no longer contributes for ongoing service to the ESPS in respect of the executive directors. Instead, WPD pays cash compensation to them individually equivalent to the value of WPD's contribution in to the fund that would have been made had they remained active members (as determined by external actuaries). Also, in 2012 three executive directors received an ex gratia payment to partially offset a liability in respect of their pension entitlement, this is shown within this line.

(vi) The three current executive directors are deferred members of the ESPS (see (v) above). At 31 March 2013, the highest paid director had accrued annual pension benefits of £474,730 (2012: £451,665). The benefits shown assume that an option to convert an element of the annual benefits to a lump sum payable on retirement is not exercised.

(vii) The independent UK non executive director is entitled to fees as determined by the appropriate Board. No emoluments are paid to US based non executive directors, who are officers of PPL, in respect of their services as directors to the groups.

(viii) In respect of the previous directors, retirement benefits accrued to two directors under a defined benefit scheme. The number of directors entitled to shares under a long-term incentive scheme during the period was two. During the period, no directors exercised options over the shares they were awarded for services to the E.ON Group. During the period, two directors exercised Stock Appreciation Rights over shares in the ultimate parent, E.ON AG, that they were awarded for services to the E.ON UK Group. During the period, the highest paid director exercised Performance Rights over shares in E.ON AG, the ultimate parent at the time, which he was awarded for services to the E.ON UK plc group.

(ix) Of the previous directors, the highest paid director had accrued pension benefits at 31 March 2011 of £142,000.



## Notes to the financial statements

For the year ended 31 March 2013

### 11. Tangible fixed assets

	Non network land & buildings £m	Distribution network £m	Fixtures & equipment £m	Vehicles & mobile plant £m	Deduct customers' contributions £m	Total £m
<b>Cost</b>						
At 1 April 2012	0.3	3,243.7	29.9	-	(679.6)	2,594.3
Additions	-	236.3	13.2	0.1	(29.0)	220.6
Transfer (to)/from WPD undertakings	-	-	(1.2)	12.9	-	11.7
Disposals and retirements	-	(13.9)	(1.6)	-	-	(15.5)
<b>At 31 March 2013</b>	<b>0.3</b>	<b>3,466.1</b>	<b>40.3</b>	<b>13.0</b>	<b>(708.6)</b>	<b>2,811.1</b>
<b>Depreciation</b>						
At 1 April 2012	0.2	857.7	6.5	-	(191.8)	672.6
Charge for the period	-	56.4	8.6	0.2	(10.9)	54.3
Transfer to WPD undertakings	-	-	(0.3)	-	-	(0.3)
Disposals and retirements	-	(13.8)	(1.6)	-	-	(15.4)
<b>At 31 March 2013</b>	<b>0.2</b>	<b>900.3</b>	<b>13.2</b>	<b>0.2</b>	<b>(202.7)</b>	<b>711.2</b>
<b>Net book value</b>						
<b>At 31 March 2013</b>	<b>0.1</b>	<b>2,565.8</b>	<b>27.1</b>	<b>12.8</b>	<b>(505.9)</b>	<b>2,099.9</b>
<b>At 1 April 2012</b>	<b>0.1</b>	<b>2,386.0</b>	<b>23.4</b>	<b>-</b>	<b>(487.8)</b>	<b>1,921.7</b>

All non network land and buildings are freehold. The net book value of land and buildings within the distribution network above is £79.6m freehold (2012 £61.9m) and £7.1m leasehold (2012 £7.3m)

Customers' contributions relate entirely to the construction of the distribution network. Transfer from WPD undertakings largely relates to the transfer of vehicles from WPD South West during the year.

Included within the Company's fixed assets are assets in the course of construction amounting at 31 March 2013 to £29.7m (2012 £24.8m) and land at a cost of £44.8m (2012 £39.6m)

## Notes to the financial statements

For the year ended 31 March 2013

### 12. Stocks

	2013 £m	2012 £m
Raw materials and consumables	2.8	2.7
Work in progress	0.1	0.3
	2.9	3.0

### 13. Debtors

	2013 £m	2012 £m
Amounts falling due within one year		
Trade debtors	68.8	63.4
Amounts owed by other WPD undertakings	55.8	114.9
Other debtors	0.5	2.1
Prepayments and accrued income	25.5	2.3
Amounts falling due after more than one year		
Other debtors	7.1	7.2
Prepayments and accrued income - pensions	42.3	-
	200.0	189.9

Amounts owed by other WPD undertakings are unsecured and are repayable on demand

## Notes to the financial statements

For the year ended 31 March 2013

### 14. Creditors

	2013 £m	2012 £m
Amounts falling due within one year		
Bank loans and overdrafts	6.0	0.1
Payments received on account	30.8	22.3
Trade creditors	6.1	3.4
Amounts owed to other WPD undertakings	8.6	7.0
UK corporation tax	16.8	9.7
Other taxation and social security	15.8	16.9
Other creditors	0.4	2.0
Accruals and deferred income	93.6	102.4
	<b>178.1</b>	<b>163.8</b>
Amounts falling due after more than one year		
Unsecured external borrowings repayable after more than five years		
£250m 6.0% sterling bond 2025	246.7	246.6
£800m 5.75% bonds 2032	787.1	786.2
	<b>1,033.8</b>	<b>1,032.8</b>

The bank loans and overdrafts are unsecured. The overdraft is repayable on demand and includes cheques issued but not yet presented. Bank loans are short term. Amounts owed to other WPD undertakings are unsecured and are repayable on demand.

Unsecured borrowings are stated net of unamortised issue costs of £5.3m (2012: £5.6m) and discount on issue of £10.9m (2012: £11.6m). These costs together with the interest expense are allocated to the profit and loss account over the term of the bonds at a constant rate on the carrying amount.

### 15. Derivative financial instruments

As at 31 March 2013 the Company held the following derivative financial instruments measured at fair value.

	2013 £m	2012 £m
Forward interest rate swaps		
Current	6.3	-

As permitted by FRS 29 "Financial Instruments: Disclosure and Presentation", full disclosure relating to derivative financial instruments is consolidated with those of the PPL WEM Holdings plc Group and is incorporated in the disclosure in the Group financial statements. An outline of the Company's financial risks and the policies and objectives pursued in relation to those risks is set out in the financial risk management section in the Directors' report.

## Notes to the financial statements

For the year ended 31 March 2013

### 16. Provisions for liabilities and charges

	Deferred taxation (Note 17) £m	Other £m	Total £m
At 1 April 2012	94.2	36.3	130.5
Arising/(released) during the period	10.4	(0.5)	9.9
Utilised during the period	-	(7.3)	(7.3)
At 31 March 2013	104.6	28.5	133.1

Other provisions at 31 March 2013 include £10.3m in relation to clearing a backlog of tree cutting (2012: £17.5m), £10.7m associated with a required change to the network (2012: £10.7m), and other items including insurance related claims. Other provisions are expected to be utilised within three years.

### 17. Deferred tax

	2013 £m	2012 £m
Accelerated capital allowances	203.1	203.1
Chargeable gain on sale of electricity supply business	-	5.5
Other timing differences	2.1	(11.7)
Undiscounted provision for deferred tax	205.2	196.9
Discount	(100.6)	(102.7)
Discounted provision for deferred tax (Note 16)	104.6	94.2

	12 months ended 31 March 2013 £m	15 months ended 31 March 2012 £m
Provision for deferred tax at beginning of period	94.2	75.5
Deferred tax charge in profit and loss account (Note 6(a))	11.8	20.0
Amount credited to statement of total recognised gains and losses	(1.4)	(1.3)
Provision for deferred tax at 31 March	104.6	94.2

Deferred tax assets are recognised for tax loss carry-forwards to the extent that the realisation of the deferred tax benefit through future taxable profits is probable. The Company did not recognise deferred tax assets of £54.9m (2012: £57.4m) in respect of capital losses amounting to £238.9m (2012: £239.1m) that can be carried forward against future taxable chargeable gains.

## Notes to the financial statements

For the year ended 31 March 2013

### 18. Called-up share capital

	2013 £	2012 £
<b>Allotted, called-up and fully paid:</b>		
100,050,000 ordinary shares of £1 each	100,050,000	100,050,000

### 19. Reserves

	Share premium account £m	Hedging reserve £m	Profit & loss account £m
At 1 April 2012	713.6	(4.2)	58.0
Profit for the financial year	-	-	166.6
Dividends paid	-	-	(77.2)
Cash flow hedges (including recycling)	-	(4.7)	-
At 31 March 2013	713.6	(8.9)	147.4

The share premium account arose on the issue of shares prior to the acquisition as settlement of intercompany balances within the group at that time

The hedging reserve is stated net of tax and relates to

- the effective portion of the cumulative net change in fair value of interest rate derivatives entered into in anticipation of the future issuance of long-term debt
- the effective portion of the value paid in respect of interest rate derivatives associated with the issuance of existing long-term debt, which is being recycled to the profit and loss account over the term of the derivatives.

### 20. Reconciliation of movements in equity shareholders' funds

	12 months ended 31 March 2013 £m	15 months ended 31 March 2012 £m
Profit for the financial period	166.6	40.4
Dividends paid	(77.2)	(982.0)
Net movement in hedging reserve	(4.7)	(4.2)
New shares issued	-	813.6
Net increase/(decrease) in equity shareholders' funds	84.7	(132.2)
Opening equity shareholders' funds	867.5	999.7
Closing equity shareholders' funds	952.2	867.5

## Notes to the financial statements

For the year ended 31 March 2013

### 21. Capital and other commitments

a) There are annual commitments under operating leases which expire

	2013 £m	2012 £m
In the first year	2.8	2.8
In the second to fifth year	0.2	4.0
In more than five years	0.1	0.2
	3.1	7.0

b) Fixed asset expenditure contracted but not provided for in the financial statements at 31 March 2013 was £11.7m (31 March 2012: £1.1m)

c) During the DPR4 period, which covered a 5 year period to 31 March 2010, DNOs were subject to a mechanism by which their management of line losses was measured and, depending on their performance, they received either financial incentives or penalties. As part of the close out of DPR4, the regulator Ofgem is currently determining the final settlement of amounts under this mechanism. Although the final values have yet to be determined, Ofgem determined that WPD West Midlands reduce its regulated income for 2013/14 by approximately £11m and final adjustments will occur in future years.

### 22. Related party transactions

The Company, a wholly-owned subsidiary undertaking, has taken the exemption available from related party disclosure requirements of FRS 8 as the financial statements of a parent company are available to the public (Note 23).

### 23. Ultimate parent undertaking

The immediate parent undertaking of the Company is WPD Midlands Holdings Limited, which is registered in England and Wales.

The smallest group in which the results of the Company are consolidated is headed by PPL WEM Holdings plc. Copies of these financial statements may be obtained from the Company's registered office as stated below.

The largest group in which the results of the Company are consolidated is that headed by PPL Corporation, which is the ultimate parent undertaking. Copies of their accounts may be obtained from Two North Ninth Street, Allentown, Pennsylvania, PA18101-1179, US.

#### Registered office:

Western Power Distribution (West Midlands) plc  
Avonbank  
Feeder Road  
Bristol BS2 0TB

Telephone 0117 933 2000  
Fax 0117 933 2001  
eMail [info@westernpower.co.uk](mailto:info@westernpower.co.uk)

Registered number 3600574