Wales & West Utilities Limited

DIRECTORS' REPORT AND FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 MARCH 2008

Registered No. 05046791

CONTENTS:

DIRECTORS AND ADVISORS

Duncan Whyte (A, R, H)	Chairman
Graham Edwards (H)	Chief Executive Officer
Martin Baggs (R)	
Stephen Box (A, H)	
Philip Garling (R)	
Howard Higgins (A, R, H)	
Alan Kadic (R)	
Charles Lynam	
Manoj Mehta (A,H)	

Edward Beckley	**(Alternate Director to Martin Baggs, Howard Higgins and Charles Lynam)**
Graeme Bevans	**(Alternate Director to Alan Kadic)**
Steven Bickerton	**(Alternate Director to Philip Garling)**
Charles Hazelwood	**(Alternate Director to Graham Edwards)**
Frederic Michel-Verdier	**(Alternate Director to Manoj Mehta)**

(A) Member of the Audit Committee
(R) Member of the Remuneration Committee
(H) Member of the Health & Safety Committee

COMPANY SECRETARY AND REGISTERED OFFICE

Christopher Talbot
Wales & West House, Spooner Close, Celtic Springs, Coedkernew, Newport NP10 8FZ

AUDITORS

PricewaterhouseCoopers LLP
1 Kingsway, Cardiff CF10 3PW

PRINCIPAL BANKERS

Barclays Bank plc

REPORT OF THE DIRECTORS

The directors have pleasure in presenting the fourth annual report to the shareholders of Wales & West Utilities Limited ("the Company"), together with the audited financial statements for the year ended 31 March 2008 as presented on pages 14 to 40

PRINCIPAL ACTIVITIES AND BUSINESS REVIEW

The Company is principally engaged in the management of gas transportation assets The Company provides gas distribution and meter work services throughout Wales and the South West of England

RESULTS AND OPERATING PERFORMANCE

The loss on ordinary activities before taxation amounted to £94 6m (2007 loss of £125 4m) The loss attributable to shareholders amounted to £106 1m (2007 £99 9m)

The results of the Company for the year ended 31 March 2008 are set out in the Profit and Loss account on page 14

The Company replaced 410km of gas mains, along with the related gas services and service pipes running from the gas mains to the properties of gas consumers at a cost of £57 7m (2007 403km at a cost of £56 1m) The work was undertaken either because mains were identified as requiring replacement under a programme defined by the Health & Safety Executive where all metallic mains within 30 metres of a dwelling are being replaced with plastic alternatives over a period of 30 years, because the overall condition of the metallic main warranted replacement or because of a request (usually through a local authority as a result of a highways project) to move the gas infrastructure A further £0 7m (2007 £0 9m) was spent on Local Transmission System replacement projects Under UK Generally Accepted Accounting Principles these costs are charged as an operating cost

In addition, the Company invested £55 1m (2007 £52 8m), against which consumers contributed £14 8m (2007 £13 7m), on expanding and improving the gas distribution network

BUSINESS REVIEW

The Company's operating performance over the past year has been good, with all standards of performance being achieved In particular, targets for mains abandoned and replaced were met, as were targets in response to reported possible gas escapes, both in one and two hour time frames The standards for achieving connections quotations and for completing connections activities within agreed timescales were also both met The numbers of complaints were 2% higher than last year

There were four lost time injuries to direct and contract labour during the year, which was one higher than the year ended 31 March 2007 This level of performance continues to place the Company at the fore-front of the gas sector and compares favourably with leading world-class organisations All of the lost time injuries were sustained through our contract partners and accordingly the direct labour workforce suffered no lost time injuries (2007 two lost time injuries), the first time that this has occurred

In addition to meeting all operational standards for the year, the Company also continued to work to improve operational efficiency

ORGANISATIONAL RESTRUCTURE

An organisational restructure was undertaken in early 2008 to allow realignment of core activities with the aim of improving the efficiency and effectiveness of the organisation This cost £11 3m and payments are expected to be incurred in the first half of the year ended 31 March 2009 The restructure resulted in a manpower reduction of 132 people at the end of the year which was achieved through a voluntary redundancy programme The new organisational structure is effective from April 2008

HISTORY AND DEVELOPMENT

The Company is a regulated gas transportation business owning and operating the principal gas distribution network in Wales and the South West of England consisting of some 32,000 kilometres of pipelines The Company operates under a Gas Transporter's licence granted by the Gas and Electricity Markets Authority and is responsible for the safety, development, maintenance and daily operation of the gas distribution network which it owns Gas is transported on behalf of approximately 30 gas shippers through the Company's distribution pipelines to around 2 4 million consumers

The Company is a private company Details of the immediate and ultimate parent companies are set out in note 26 to the statutory financial statements

BUSINESS ENVIRONMENT

The Gas Distribution and Transmission Network in Great Britain comprises the National Transmission System and eight gas distribution networks The National Transmission System is owned and operated by companies within the National Grid plc Group

The Company operates the Wales and South West local distribution zones of one of the gas distribution networks Three other distribution networks are owned by independent operators National Grid retained the remaining four local gas distribution networks Together these companies represent the great majority of the gas transmission and distribution network in Great Britain

There are however other independent gas transporters who operate within the principal area of the Company's operation and the Company has contractual arrangements in place with them to ensure the safe passage of gas to their networks

In addition to its gas distribution role, the Company also has obligations under its gas transporter's licence to

- provide 24 hour emergency response to all public reported gas escapes in Wales and South West England, irrespective of the cause (the significant majority of which are unrelated to the Company's distribution network)
- connect gas consumers to the distribution network, unless the consumer chooses to use another party to provide the connection, and
- to provide meters to certain consumers if the consumer's gas supplier has not made alternative arrangements

And under contractual arrangements with gas suppliers to

- provide and maintain gas meters for some consumers

REGULATORY ENVIRONMENT

The gas distribution business of the Company is regulated by the Office of Gas & Electricity Markets (Ofgem) Ofgem operates under the direction and governance of the Gas and Electricity Markets Authority, which makes all major decisions and sets policy priorities for Ofgem The mechanism for regulation of the Company's activities in gas distribution and metering is derived from

- the Gas Act 1986 (as amended),
- the terms of its gas transporter's licence granted under Section 7 of this Act, and
- the Utilities Act 2000

The Company is also regulated by the Health and Safety Executive

As a regulated business the Company is subject to price controls set by Ofgem which define its allowed revenues The price control under which the Company operated for the year to 31 March 2008, which the Company accepted in January 2007, expired at that date This control defined allowed revenue in respect of operating expenditure, capital expenditure, replacement expenditure and a return on the Company's investment in the gas infrastructure asset In January 2008 the Company accepted Ofgem's Final Proposals for the five year price control for the period from 1 April 2008 to 31 March 2013

KEY PERFORMANCE MEASURES

The Company uses a number of key measures of operational and financial performance to plan and monitor its business activities which are principally focused on the safe and effective operation of the gas network infrastructure asset Measures of operational performance include

- Process safety – safety of the gas transportation assets,
- Occupational safety & health - Injuries, near misses and ill health,
- Environment – Waste disposal, energy usage and use of natural resources,
- The management of controllable costs in relation to the regulated business,
- The achievement of service levels and the minimisation of complaints,
- Achievement of capital and replacement programme targets and cost efficiency, and
- The reliability of the gas distribution network and other customer facing quality of service measures

The Directors believe that safety is paramount and, as a fundamental part of this, that all work related injuries and illnesses are preventable Consequently the Company measures the level of injuries, incidents and near misses as a key operational performance indicator In addition, process safety measures have been devised to measure both the 'health' of the assets and their impact on the environment and the communities in which the Company works Contractor performance is measured in the same way as direct employees

Operational reliability is a core measure of the Company's success, and it is fundamental to the Company's relationships with Ofgem and the public Reliability of the gas distribution network is monitored in a number of ways, including the number and duration of interruptions to consumers' gas supplies The Company is required by Ofgem to meet a number of different service targets ("Overall Standards"), including attendance at gas escapes, notifying consumers in advance of planned interruptions and responding to complaints The Company's licence also requires it to meet certain service targets for connections Performance against these standards is reported to senior management every month and is reportable to Ofgem on a quarterly basis Compensation payments are made to consumers under the Gas (Standards of Performance) Regulations 2005, in the regrettable event that certain service standards are not met

The Company measures service quality to assess the performance of management and staff in serving consumers, including a quarterly survey which is undertaken by an independent market research company, the results of which are published on the Company's website and are reported to Ofgem

All key regulatory standards of performance were achieved in the year to 31 March 2008

Key operational performance measures were,

- 97% (2007 97%) targets for responding to gas escapes in both 1 hour for uncontrolled escapes 98 0% (2007 97 2%) and 2 hour for controlled escapes 99 3% (2007 98 7%) timeframes met
- the regulatory standards for Connections (quotations & physical completion of jobs) activities achieved well within target timescales,
- response to complaints well within the target regulatory standard,
- maintain a low level of overall customer complaints (2% increase on prior year) which was achieved against an 18% reduction in the previous year, and
- 85% (2007 50%) reduction in complaints to Energywatch

Key financial performance measures were,

- Operating cash flow, including management of working capital, and
- controllable costs

HEALTH, SAFETY AND ENVIRONMENT

Safety

The Company's objective is to achieve zero work-related injuries, zero work-related ill health and zero injuries to the public Over the last year, there were four (direct labour nil, contract labour four) (2007 three direct labour two, contract labour one) lost time injuries between direct and contract labour, giving a 12 month frequency rate of 0 10 LTI's/100,000 hours worked (2007 0 076 LTI's/100,000 hours worked) This represents a 30% increase (2007 50% reduction) during the year compared with the year ended 31 March 2007 This rate compares very favourably with other industry comparators that are available, such as electricity distribution (0 25 LTI's/100,000 hours worked)

The Company continues to make progress in the management of occupational illnesses with a comprehensive health surveillance programme for industrial employees

The safety challenge is significant With a deployed work force (including contractors) of around 2,000, a multi million pound replacement programme and the Company's core role of managing the safe and secure delivery of gas, the Company meets this challenge by having a comprehensive management system designed and certified to standards such as ISO 14001, with a structured risk management process at its core

The Company believes that its safety performance leads the sector and that valued position is targeted at being maintained through continued, vigilant implementation of its health, safety and environmental procedures Nurturing a safety aware culture within the Company's workforce that sees clear accountability resting with line management, employees and contract partners is a key element of the Company's successful record

Environment

The Company is also proud of its environmental achievements In addition to maintaining certification to ISO 14001, it retained the prestigious Green Dragon Award for the Company's Welsh region at the highest level – an award only achieved by a handful of companies By utilising and developing industry-wide best practices, the Company has reduced its environmental impact Key areas for focus have been climate change, the disposal of waste to land fill and the use of quarried stone Protecting the environment is a key focus for the Company going forward, constantly looking for ways to minimise the environmental impact of its past, present and future activities

The Company continues to manage its portfolio of contaminated land These sites are principally former manufacturing gas plants and can sometimes have a complex mix of contamination dating back over 100 years The Company's remediation programme has a main focus on managing environmental risk

PRINCIPAL RISKS AND UNCERTAINTIES

The management of the business and the execution of the Company's strategy are subject to a number of risks The key business risks facing the Company are set out below

Operational

- Maintenance of the gas distribution network and security of supply,
- Health & Safety compliance,
- Appropriate investment in the network asset, and
- Meeting mains replacement targets

Regulatory

- Compliance with the Company's licence obligations and standards of service, and
- Impact of future price controls determined by Ofgem, including the effect of incentive mechanisms

Employee

- Retention of key individuals or the ability to recruit people with the right experience and skills from the local community

Risks are reviewed by the board and senior management and appropriate processes put in place to monitor and mitigate them If more than one event occurs, it is possible that the overall effect of such events would compound the possible adverse effects on the Company

FINANCIAL RISK MANAGEMENT

The Company's operations expose it to a variety of financial risks that include the effects of changes in debt and commodity market prices, credit risk, liquidity risk and interest rate risk The Company has in place a risk management programme that seeks to limit the adverse effects on the financial performance of the Company by monitoring levels of debt finance and related finance costs The Company also uses derivative financial instruments to manage interest rate costs

Given the size of the Company, the Directors have not delegated the responsibility of monitoring financial risk management to a sub-committee of the Board The policies set by the Board are implemented by the Company's finance department

Commodity Price risk

The Company is exposed to commodity price risk through the purchase of "shrinkage gas" as a result of its operations Shrinkage gas is that gas which the Company consumes during its operational activity and comprises gas used by the gas distribution business, the gas which leaks from the distribution network and gas stolen from the network This risk is managed through appropriate commodity purchase in the forward market

Credit risk

The Company has implemented policies that require appropriate credit checks on potential customers before sales are made The amount of exposure to any individual counterparty is subject to a limit, which is reassessed on a regular basis

The amount of credit given to Gas Shippers is governed by Uniform Network Code ("UNC") regulations and guidelines This provides for defined levels of unsecured credit with Gas Shippers based on Investment Grade Ratings ("IGRs") with any excess credit amounts being secured by Letters of Credit, Parent Company Guarantees or by way of Prepayment

The value at risk is monitored on a daily basis and is again regulated by UNC criteria allowing a maximum credit limit usage of 100% (2007 85%) which, if exceeded, allows the Company to apply sanctions

The Company's overall exposure is also monitored and approved having regard to the levels of exposure within each IGR category

Financing and Interest rate cashflow risk

The Company actively maintains long term debt finance that is designed to ensure the Company has sufficient available funds for operations

The Company has both interest bearing assets and interest bearing liabilities Interest bearing assets are cash, which bear interest at variable rates The Company has a policy of hedging through interest rate swaps in order to fix interest rates and give greater certainty over future cashflows

The primary financing activity during the year was the restructure of the Company's hedging arrangements, whereby the Company entered into £964m of index-linked swaps with maturities ranging between 2023 and 2039, in line with the strategy approved by the Board (note 13(a))

FINANCIAL REVIEW

Basis of accounting

The accounts present the Company's results for the period ended 31 March 2008 and the financial position as at 31 March 2008 and 2007 They have been prepared using the accounting policies shown on pages 18 to 21, in accordance with generally accepted accounting practices in the United Kingdom

There were no changes in accounting policies adopted during the year

Segmental reporting

In addition to providing the overall results and financial position in the financial statements, the Company provides a breakdown of those results and balances into a number of different business segments as required by the License within the Regulatory Accounts

Liquidity, resources and capital expenditure

Net cash inflow from operations amounted to £86 6m (2007 £62 9m), and was augmented by new long term loans of £50 0m (2007 £39 0m)

Capital purchases absorbed net cash of £41 8m (2007 £35 2m) and net financing costs amounted to £93 8m (2007 £68 3m)

Cash flow forecasting

Both short term and long term cashflow forecasts are produced frequently to assist in identifying the liquidity requirements of the Company

Debt

Details of net debt are disclosed in note 9 and 10 and gross debt in note 12 Details of the Company's approach to financial risk management are set out in the Report of the Directors on page 6

At 31 March 2008, and throughout the year, the Company, together with its immediate parent company MGN Gas Networks (Senior Finance) Ltd, held a senior implied Baa1 credit rating from Moodys

Shareholder funds

Shareholder funds at 31 March 2008 amounted to a deficit of £294 0m (2007 £182 2m) as a result of a retained loss of £106 1m (2007 £99 9m) and reserves movement on the Pensions provision loss of £5 7m (2007 loss £20 6m)

The Directors consider that the company has performed satisfactorily during the year

Details of the ownership of the Company are included in note 26 Details of movements in the authorised and issued share capital of the Company are included in Note 17

DIVIDEND ON ORDINARY SHARES

The Directors do not recommend the payment of a dividend (2007 Nil) in respect of the period

FUTURE DEVELOPMENTS

The Company does not envisage any changes in the activity of the Company for the foreseeable future Other than those matters referred to above, there were no significant developments within the Company that occurred during the financial year under review

FIXED ASSETS

Freehold land and buildings are carried in the accounts at fair value of £1 8m (2007 £1 9m)

In the opinion of the Directors there was no significant difference between the book values of property and market values at 31 March 2008

Investment in the network is essential for ensuring the security of the gas supply and the safety of the public Gross capital expenditure in the Company's network was £55 1m (2007 £52 8m) offset by capital contributions of £14 8m (2007 £13 7m) and net replacement expenditure was £58 4m (2007 £57 0m) in the year to 31 March 2008

DIRECTORS

The names of the current directors of the Company are shown on page 1

Changes in directors during the period up to the date of signature of the statutory accounts are shown below, all other directors served throughout the period

Christopher Koski		Resigned 13 April 2007
Graeme Bevans (Alternate)	Appointed 13 April 2007	
Alan Kadic	Appointed 13 April 2007	
Martin Stanley		Resigned 17 May 2007
Martin Baggs	Appointed 17 May 2007	
Raymond A Clamp		Resigned 6 July 2007
James Dickson	Appointed 6 July 2007	Resigned 22 May 2008
Peter Antolik		Resigned 31 July 2007
Charles Lynam	Appointed 31 March 2008	
Edward Beckley (Alternate)	Appointed 1 April 2008	
Manoj Mehta	Appointed Alternate 1 April 2008 Appointed full director 22 May 2008	
Frederic Michel-Verdier (Alternate)	Appointed 22 May 2008	

DIRECTORS' SERVICE CONTRACTS AND REMUNERATION

Details of directors' remuneration are set out in note 2(a)

DIRECTORS' INTERESTS

There were no significant contracts subsisting during or at the end of the year with the Company in which any director is or was materially interested (other than service contracts)

None of the directors has or has had a beneficial interest in the shares of the Company

POLICY ON THE PAYMENT OF CREDITORS

It is the Company's policy to comply with terms of payment agreed with suppliers Where payment terms are not negotiated the Company endeavours to adhere with the suppliers standard terms

EMPLOYMENT POLICIES

The Company recognises that its employees are key to both the present and future success of the Company and supports the fundamental belief that to maximise the potential of every individual there must be -

- Investment in training and development,
- A supportive working environment, and
- Employee participation and involvement in business matters

To this end the Company continually evolves a framework of comprehensive policies and all employees have the opportunity to discuss their individual performance and development in a focused and proactive way

The Company seeks to maximise staff potential by encouraging employees to consider internal opportunities as part of their personal development This can only be achieved with knowledge of the Company's business aims and objectives, and keeping employees up to date with the Company's news and views continues to be a high priority The in-house newspaper supports this endeavour and provides a wide range of information

The Company continues to formally consult employees at all levels in the spirit of partnership and co-operation and the use of employee opinion and attitude surveys will provide the Company with valuable information upon which to base future policy decisions

The Company offers equality of opportunity and support for disabled employees and maintains good links with external organisations to encourage involvement in the workplace of disabled members of the wider community

The Company's policy for the employment of disabled persons gives full and fair consideration to all applications for employment made by such persons, having regard to their aptitudes and abilities and to the Company's operational requirements Once employed, a career plan is developed so as to ensure suitable opportunities for each disabled person Arrangements are made, where possible, for retaining employees who become disabled, to enable them to perform work identified as appropriate to their aptitudes and abilities in line with the Company's operational requirements

Training & development

The Company has consistently sought to recruit and retain the best employees in its local geography in order to provide the level of service which is expected

The Company measures success in this area through employee retention The Company has had a turnover rate of 5 0%, in the year to 31 March 2008 (2007 5 6%) before the voluntary redundancy programme The Chartered Institute of Personnel & Development stated that the average in UK industry during 2007 was 18 1% (2006 18 3%)

To improve retention rates the Company has continued its focus on Succession Planning and Talent Management This ensures that key skill and knowledge workers are retained and that there is a plan to replace them upon retirement

The Apprenticeship Programme has been further developed and also extended to include Emergency Services This is a 3-4 year training period, depending on the course of study undertaken and there are now 3 in-house purpose built training centres for our Apprentices to develop their practical and technical skills The use of these centres was extended to include other technical training in 2007 This programme continues into 2008/09

During the year the company employed 25 apprentices Refreshing the Industrial workforce is seen as being important The age profile of the Industrial workforce is high and the Company will see a large number of leavers' during the next 5 years and beyond The apprentices were recruited into the areas of "Emergency", "Mechanical Engineering" and "Electrical & Instrumentation" – Key areas where skills are not readily available in the external market and training times can be 4 years or more Ensuring continuity to the key skills required within the Industry and enabling a full and proper knowledge transfer to take place will ensure that the Company is well placed to effectively undertake this work going forward The recruitment brings to 34 the number of apprentices employed in the last two years and a further 25 are planned to be taken on in 2008/9

Additionally during 2007/08 WWU employed directly a further 100 people previously provided by our contract partners, which has tangible benefits to both the employees and company, not least, the fact that it further refreshes the workforce, as this recruited population generally have a younger age profile A total of 160 people have now been directly employed and a further recruitment event is planned for 2008/9

CONTRIBUTIONS FOR CHARITABLE AND POLITICAL PURPOSES

During the year, there have been no political donations, and charitable donations amounted to £34,800 (2007 £25,600) Donations in excess of £200 were made to

Age concern	£1,000
Breast Cancer Awareness	£700
Cancer Research	£2,147
Community Foundation in Wales	£22,000
Flint & Holywell Rotary Club	£300
Hop, Skip & Jump Cotswold	£300
Hope House Childrens' Hospice	£400
Macmillan Cancer Relief	£500
Marie Curie Cancer Care	£350
NSPCC	£341
Oxfam	£300
SportsAid	£2,500
St Davids' Hospice	£300
St John Ambulance	£300
St Mellon Parish Church	£300
St Peters' Hospice	£300
Ty Hafan Childrens' Hospice for Wales	£1,654
Wellspring	£300

GOING CONCERN

The Company's accounts have been prepared on the basis that the Company is a going concern In arriving at their decision to prepare the accounts on a going concern basis, the directors have reviewed the Company's budget for 2008/09 and medium term business plans for 2009/10 to 2012/13 including capital expenditure plans This included consideration of the cash flow implications of the plans and comparing these with the Company's cash resources and committed borrowing facilities

REGULATORY ACCOUNTS

The Gas Transporters Licence, under which the Company operates, requires specific accounting statements to be published Copies of the regulatory accounts for the Company will be available from the Company Secretary after 30 September 2008

AUDITORS

Pursuant to Section 386 of the Companies Act 1985, an elective resolution was passed on 8 June 2006 resolving that the Company dispense with the requirement to appoint auditors annually

In the case of each of the persons who are directors at the time when the report is approved under section 234A of the Companies Act 1984

- so far as the director is aware, there is no relevant audit information of which the company's auditors are unaware, and
- the director has taken all the steps that he ought to have taken as a director in order to make himself aware of any relevant audit information and to establish that the company's auditors are aware of that information

By Order of the Board

C Talbot
Company Secretary
23 May 2008

STATEMENT OF DIRECTORS' RESPONSIBILITIES FOR THE FINANCIAL STATEMENTS

The directors are required by the Companies Act 1985 to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company as at the end of the financial year and of the profit/loss of the Company for the year In preparing the financial statements, the directors are required to

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

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and to enable them to ensure that the financial statements comply with the Companies Act 1985 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

By Order of the Board

C Talbot
Company Secretary

23 May 2008

REPORT OF THE INDEPENDENT AUDITORS TO THE MEMBERS OF WALES & WEST UTILITIES LIMITED

We have audited the financial statements of Wales & West Utilities Limited for the year ended 31 March 2008 which comprise the Profit and Loss Account, the Balance Sheet, the Cash Flow Statement, the Statement of Total Recognised Gains and Losses and the related notes on pages 14 to 40 These financial statements have been prepared under the accounting policies set out therein

Respective responsibilities of directors and auditors

As described in the Statement of Directors' Responsibilities the Company's directors are responsible for the preparation of the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice)

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland) This report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985 We report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements We also report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it

Basis of audit opinion

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

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

Opinion

In our opinion

- the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the Company's affairs as at 31 March 2008 and of its loss and cash flows for the year then ended,
- the financial statements have been properly prepared in accordance with the Companies Act 1985, and
- the information given in the Directors' Report is consistent with the financial statements

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
Cardiff
23 May 2008

PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDED 31 MARCH 2008

	Note	2008 £m	2007 £m
Turnover:			
Continuing operations		**277.7**	233 8
Net operating costs	1(a)	**(260.2)**	(234 3)
Operating profit before depreciation and exceptional item		**96.2**	52 0
Exceptional item	1(b)	**(11.3)**	-
Depreciation	5	**(67.4)**	(52 5)
Operating profit/(loss)		**17.5**	(0 5)
Operating profit/(loss):			
Continuing operations		**17.5**	(0 5)
Dividends received		**0.2**	-
Interest receivable	3(a)	**29.0**	9 3
Other finance income	16(c)	**16.5**	-
Other finance income ~ net pension	25	**3.9**	3 9
Interest payable and similar charges	3(b)	**(161.7)**	(138 1)
Loss on ordinary activities before taxation		**(94.6)**	(125 4)
Taxation	4	**(11.5)**	25 5
Loss attributable to ordinary shareholders		**(106.1)**	(99 9)
Dividends on ordinary shares		-	-
Retained loss for the year	18	**(106.1)**	(99 9)

STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES
FOR THE YEAR ENDED 31 MARCH 2008

	2008 £m	2007 £m
Loss for the financial year attributable to ordinary shareholders	**(106.1)**	(99 9)
Actuarial loss on pension scheme (note 25)	**(5.7)**	(20 6)
Total recognised gains and losses relating to the year	**(111.8)**	(120 5)

There are no material differences between the profit on ordinary activities before taxation and the retained loss for the year stated above and their historical cost equivalents

RECONCILIATION OF MOVEMENTS IN SHAREHOLDERS' FUNDS
FOR THE YEAR ENDED 31 MARCH 2008

	2008 £m	2007 £m
Total recognised losses for the year	**(111.8)**	(120 5)
Net decrease in shareholders' funds	**(111.8)**	(120 5)
At 1 April	**(182.2)**	(61 7)
At 31 March	**(294.0)**	(182 2)

BALANCE SHEET AT 31 MARCH 2008

	Note	2008 £m	2007 £m
Fixed assets			
Tangible assets	5	**1,275.0**	1,287 5
Investments	6	**0.1**	0 1
		1,275.1	1,287 6
Current assets			
Stocks and work in progress	7	**2.6**	2 7
Debtors	8	**56.2**	42 6
Cash at bank and in hand	21	**27.3**	26 9
		86.1	72 2
Current liabilities			
Creditors amounts falling due within one year	9(a)	**(529.8)**	(485 6)
Net current liabilities		**(443.7)**	(413 4)
Total assets less current liabilities		**831.4**	874 2
Creditors: amounts falling due after more than one year	9(b)	**(1,046.6)**	(956 8)
Provisions for liabilities and charges	16	**(48.6)**	(65 3)
Net liabilities before pension liability		**(263.8)**	(147 9)
Pension liability	25	**(30.2)**	(34 3)
Net liabilities including pension liability		**(294.0)**	(182 2)
Capital and reserves			
Called up share capital	17	**30.7**	30 7
Reserves	18	**(324.7)**	(212 9)
Equity shareholders' funds		**(294.0)**	(182 2)
Total shareholders' funds		**(294.0)**	(182 2)

The financial statements on pages 14 to 40 were approved by the Board of Directors on 23 May 2008 and were signed on its behalf by

Duncan Whyte
Chairman

Graham Edwards
Chief Executive Officer

CASHFLOW STATEMENT
FOR THE YEAR ENDED 31 MARCH 2008

	Note	2008 £m	2007 £m
Operatıng actıvities			
Net cash ınflow from contınuıng operatıng actıvıtıes	19	86.6	62 9
Net cash inflow from operating activıtıes		**86.6**	62 9
Returns on investments and servıcing of finance			
Dıvıdends receıved		0.2	-
Interest receıved		17.1	5 9
Interest paıd		(111.1)	(74 1)
Interest element of finance leases		-	(0 1)
Net cash outflow from returns on investments and servıcing of finance		(93.8)	(68 3)
Taxation			
UK corporatıon tax paıd		-	-
		-	-
Investing activıties			
Purchase of tangıble fixed assets		(58.0)	(50 0)
Capıtal contrıbutıons receıved		14.8	13 7
Proceeds of dısposal of tangıble fixed assets		0.6	1 1
Grants and contrıbutıons receıved		0.8	-
Net cash outflow from ınvesting activities		(41.8)	(35 2)
Net cash outflow before financing and treasury activıtıes		(49.0)	(40 6)
Fınancing and treasury activitıes			
New long term loans	20	50.0	39 0
Capıtal payments under finance leases	20	(0.6)	(1 4)
Net cash ınflow from financıng and treasury actıvıties		49.4	37 6
Increase/(decrease) ın cash and cash equivalents	21	0.4	(3 0)

PRINCIPAL ACCOUNTING POLICIES

The financial statements have been prepared in accordance with Accounting Standards applicable in the United Kingdom and comply with the Companies Act 1985 A summary of the principal Company accounting policies, which have been consistently applied, is shown below

CHANGES IN ACCOUNTING POLICY

There have been no changes in accounting policy during the year

BASIS OF ACCOUNTING

These financial statements have been prepared in accordance with the historical cost convention as modified for the fair valuation exercise undertaken on the acquisition of the gas distribution business and in respect of the valuation of pension assets and liabilities

The Directors are satisfied that the Company has adequate resources to continue in operational existence for the foreseeable future For this reason they adopt the going concern basis in the preparation of these financial statements

ACQUISITIONS AND DISPOSALS

The results of businesses acquired during the year are dealt with in the financial statements from the date of acquisition of those businesses Where appropriate, adjustments are made to bring different accounting policies of newly acquired companies into line with the existing Company accounting policies

Goodwill arising from the purchase of businesses, representing the excess of the fair value of the purchase consideration (including costs of acquisition) over the fair value of net assets acquired, is amortised over its expected future economic life

RELATED PARTY TRANSACTIONS

The Company is a 100% owned subsidiary of MGN Gas Networks (Senior Finance) Limited and is included in the consolidated financial statements of MGN Gas Networks (UK) Ltd Consequently, under the terms of FRS 8 "Related Party Transactions", the Company is exempt from disclosing related party transactions with entities that are part of the MGN Gas Networks (UK) Limited group

TURNOVER

Turnover represents the sales value derived from the distribution of gas together with the sales value derived from the provision of other services to customers during the year and excludes Value Added Tax

Turnover from the distribution of gas is partially derived from the value of units supplied during the year and includes an estimate of the value of units supplied between the date of the last meter reading and the year end No liability is recognised when revenues received or receivable exceed the maximum amount permitted by regulatory agreement and reductions will be made to future prices to reflect any over-recovery

TANGIBLE FIXED ASSETS AND DEPRECIATION

Tangible fixed assets, which include assets in which the Company's interest comprises legally protected statutory or contractual rights of use, are included in the balance sheet at their cost less accumulated depreciation Cost includes payroll and finance costs incurred which are directly attributable to the construction of tangible fixed assets

Fixed assets acquired with the acquisition of the Wales & West gas distribution business are included at fair value

Additions represent the purchase or construction of new assets and extensions or significant increases in the capacity of existing tangible fixed assets Contributions received towards the cost of tangible fixed assets are included in creditors as deferred income and amortised on a straight line basis to the profit and loss account over the estimated economic lives of the assets

No depreciation is provided on freehold land and assets in the course of construction Other tangible fixed assets are depreciated, principally on a straight line basis, at rates estimated to write off their book values over their estimated useful economic lives In assessing estimated economic lives, which are reviewed on a regular basis, consideration is given to any contractual arrangements and operational requirements relating to particular assets Unless otherwise determined by operational requirements, the depreciation periods for the principal categories of tangible fixed assets are, in general, shown below

Replacement expenditure represents the costs of planned maintenance of mains and services assets by replacing or lining sections of pipe This expenditure is principally undertaken to repair and to maintain the safety of the network and is written off as incurred Expenditure which enhances the performance of the mains and services assets is treated as an addition to tangible fixed assets

Principal depreciation periods are	
Freehold buildings	up to 50 years
Leasehold properties	over the period of the lease
Gas distribution network assets	
Mains, services and regulating equipment	30 to 65 years
Storage	40 years
Meters	10 to 33 years
Vehicles, mobile plant and equipment	3 to 10 years

Assets in the course of construction are not depreciated until commissioned All assets are depreciated on a straight line basis over their estimated economic life

IMPAIRMENT OF FIXED ASSETS

Impairments of fixed assets are calculated as the difference between the carrying values of the net assets of income generating units, including, where appropriate, investments and goodwill, and their recoverable amounts Recoverable amount is defined as the higher of net realisable value or estimated value in use at the date the impairment review is undertaken Net realisable value represents the net amount that can be generated through sale of the assets Value in use represents the present value of expected future cashflows discounted on a pre-tax basis, using the estimated cost of capital of the income generating unit

Impairment reviews are carried out if there is some indication that an impairment may have occurred, or where otherwise required, to ensure that fixed assets are not carried above their estimated recoverable amounts

Impairments are recognised in the profit and loss account and, where material, are disclosed as exceptional

LEASED ASSETS

Where assets are financed by leasing arrangements which transfer substantially all the risks and rewards of ownership of an asset to the lessee (finance leases), the assets are treated as if they had been purchased and the corresponding capital cost is shown as an obligation to the lessor Leasing payments are treated as consisting of a capital element and finance costs, the capital element reducing the obligation to the lessor and the finance charges being written off to the profit and loss account over the period of the lease in reducing amounts in relation to the written down amount The assets are depreciated over the shorter of their estimated useful life and the lease period

All other leases are regarded as operating leases Rental costs arising under operating leases are charged to the profit and loss account in the year to which they relate

GRANTS, CUSTOMER CONTRIBUTIONS AND INFRASTRUCTURE CHARGES

Grants, customer contributions and infrastructure charges relating to gas infrastructure assets and expenditure on other fixed assets are treated as deferred income and recognised in the profit and loss account over the expected useful economic lives of the related assets

Certain contributions noted above are wholly or partially refundable if an agreed volume of gas is distributed to them Such contributions are included in provisions until there is no further liability to make refunds

INVESTMENTS

Long term investments held as fixed assets are stated at cost less amounts written off or provided to reflect permanent diminutions in value Those held as current assets are stated at the lower of cost and net realisable value

STOCKS AND WORK IN PROGRESS

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

COSTS OF RAISING FINANCE

Under the provisions of FRS4 "Capital Instruments", costs associated with the raising of relevant finance are accounted for as a deduction from the amount of the consideration received The costs are then amortised over the life of the instrument

DECOMMISSIONING AND ENVIRONMENTAL COSTS

Decommissioning and environmental costs, based on discounted future estimated expenditures, are provided for in full and where appropriate a corresponding tangible fixed asset or regulatory asset is also recognised The unwinding of the discount is included within the profit and loss account as a financing charge

FINANCIAL INSTRUMENTS

Derivative financial instruments ("derivatives") are used by the Company for the management of interest rate exposures and commodity price risks in respect of expected gas usage The principal derivatives used include interest rate swaps and forward purchases relating to the purchase of gas

All transactions are undertaken, or maintained, with a view to providing a commercial hedge of the interest or commodity price risks associated with the Company's underlying business activities and the financing of those activities Amounts payable or receivable in respect of interest rate swaps are recognised in the profit and loss account over the economic lives of the agreements or underlying position being hedged, either within net interest or disclosed separately where deemed exceptional

Those derivatives relating to interest rates that are directly associated with a specific transaction and exactly match the underlying cashflows relating to the transaction are accounted for on the basis of the combined economic result of the transaction including the related derivative

PENSION COSTS

The Company operates defined contribution and defined benefit pension schemes.

The pension costs in respect of the defined contribution pension schemes comprise contributions payable in respect of the period

The assets of the defined benefit scheme are measured using closing market values Pension scheme liabilities are measured using the projected unit method and discounted at the current rate of return on a high quality corporate bond of equivalent term and currency to the liability

The increase in the net present value of the liabilities of the defined benefit scheme expected to arise from employee service in the period is charged to operating profit The net of the expected return on the scheme's assets and the increase during the period in the present value of the schemes' liabilities, arising from the passage of time, are included in net interest payable or other finance income, as appropriate

Actuarial gains and losses are recognised in the statement of total recognised gains and losses

DEFERRED TAXATION

Provision is made for deferred taxation, using the liability method, on all material timing differences to the extent that it is probable that a liability or asset will crystallise

Deferred tax assets are only recognised to the extent that they are considered recoverable

Deferred tax balances are not discounted

EXCEPTIONAL ITEMS

These are items of an unusual or non-recurring nature incurred by the Company and include restructuring costs and one off costs arising from termination of the finance swap arrangements

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 2008

1 **(a) Net operatıng costs**

Net operatıng costs ınclude

	Note	2008 £m	2007 £m
Contınuıng operatıons			
Staff costs	2(b)	**60.7**	54 3
Own work capıtalısed		**(14.4)**	(11 7)
Depreciatıon			
Own assets	5	**67.0**	52 3
Assets held under finance leases	5	**0.4**	0 9
Less amortısatıon of customer contrıbutıons		**(1.8)**	(0 5)
Profit on dısposal of fixed assets		**(0.3)**	(0 3)
Replacement expendıture		**58.4**	57 0
Rentals under operatıng leases			
Hıre of plant and equıpment		**1.3**	1 0
Other		**1.7**	1 1
Exceptıonal ıtems ~ restructurıng costs	1(b)	**11.3**	-

Own work capıtalısed ıncludes dırect labour and ancıllary costs

(b) Exceptıonal ıtem

The exceptıonal ıtem ıs the cost of undertakıng the voluntary severance programme entered ınto by the Company at the end of the year

(c) Auditor remuneration

Services provıded by the auditor

Durıng the year the Company obtaıned the followıng servıces from the group's audıtor at costs as detaıled below

	2008 £000	2007 £000
Audıt Servıces		
Fees payable to company audıtor for the audıt	**70.0**	70 0
Non Audıt Servıces		
Fees payable to the company's audıtor and ıts assocıates for other servıces		
Other servıces pursuant to legıslatıon	**25.0**	25 0
Tax Servıces	**7.0**	7 0
	102.0	102 0

	2008 £000	2007 £000
Fees ın respect of the pensıon scheme		
Audıt of pensıon scheme	**9.0**	9 0
	9.0	9 0

2 Directors and employees

(a) Directors' emoluments and interests

Directors' emoluments

	2008 £000	2007 £000
Fees	**130.0**	80 0
Salary payments (including benefits in kind)	**282.1**	251 0
Performance related bonus	**385.0**	250 0
Pension contributions	**32.2**	22 5
Contributions in lieu of pension	**35.0**	38 5
	864.3	642 0

One director is a member of the defined contribution section of the Company pension scheme All other directors make their own pension arrangements

The performance bonus is payable in instalments, with two thirds payable in the July of the year following the year end and the balance being payable in two equal annual instalments conditional on the director remaining in office on the payment date

No director had any interest over shares in the Company

Highest paid director

	2008 £000	2007 £000
Salary payments (including benefits in kind)	**282.1**	251 0
Performance related bonus	**385.0**	250 0
Pension contributions	**32.2**	22 5
Contributions in lieu of pension	**35.0**	38 5
	734.3	562 0

(b) Staff costs

	2008 £m	2007 £m
Wages and salaries	**46.2**	41 2
Social security costs	**4.0**	3 8
Pension costs	**10.5**	9 3
	60.7	54 3

Of the above, £8 3m (2007 £8 9m) has been charged to capital

(c) Average monthly number of employees during the year (including directors)

	2008 Number	2007 Number
Regulated gas distribution activities	**1,386**	1,281
Other activities	**2**	2
	1,388	1,283

3 Interest

(a) Interest receivable and other finance income

	2008 £m	2007 £m
On interest rate swaps	28.0	8 6
Other interest receivable	1.0	0 7
	29.0	9 3

(b) Interest payable and similar charges

	2008 £m	2007 £m
On external loans	83.5	64 3
On group loans	74.2	70 7
On finance leases	-	0 1
On unwinding of discounts on provisions (note 16)	1.5	1 9
Other	2.5	1 1
	161.7	138 1

4 Taxation

(a) Analysis of charge/(credit) in the year

	2008 £m	2007 £m
The charge/(credit) for taxation is made up as follows:		
Current tax		
UK corporation tax on profits of the year	(6.5)	(16 2)
Adjustments in respect of previous periods	18.0	(9 3)
Total current tax (Note 4(b))	11.5	(25 5)
Deferred tax		
Origination and reversal of timing differences	-	-
Total deferred tax (Note 16)	-	-
Total tax on profit on ordinary activities	11.5	(25 5)

The £11 5m (2007 £25 5m) reflects amounts due to/(from) Group undertakings in respect of group relief surrendered for the year ended 31 March 2008

4 Taxation (continued)

(b) Factors affecting the current tax charge /(credit) for the year

The current tax assessed for the year is different to the standard rate of corporation tax in the UK of 30% The differences are explained below

	2008 £m	2007 £m
Loss before tax	(94.6)	(125 4)
Loss multiplied by standard rate of corporation tax in the UK of 30% (2007 30%)	(28.4)	(37 6)
Effects of:		
Prior year charge/(credit)	18.0	(9 3)
Permanent differences	15.1	4 5
Deferred tax asset not recognised	6.4	17 3
FRS17 deferred tax movement not recognised	0.4	(0 4)
Current tax charge/(credit) for year (Note 4(a))	**11.5**	(25 5)

5 Tangible fixed assets

	Freehold land and buildings £m	Leasehold land and buildings £m	Gas distribution network assets £m	Vehicles, plant and equipment £m	Assets under construction £m	Total £m
Cost or valuation						
At 1 April 2007	1 9	1 3	1,307 4	58 5	23 2	**1,392.3**
Additions	0 1	-	-	-	55 0	**55.1**
Disposals	(0 2)	-	-	(0 1)	-	**(0.3)**
Transfers in year	-	0 2	47 3	17 1	(64 6)	-
At 31 March 2008	**1.8**	**1.5**	**1,354.7**	**75.5**	**13.6**	**1,447.1**
Accumulated depreciation						
At 1 April 2007	-	-	95 6	9 2	-	**104.8**
Charge for the year	-	0 1	54 2	13 1	-	**67.4**
Disposals	-	-	-	(0 1)	-	**(0.1)**
At 31 March 2008	-	**0.1**	**149.8**	**22.2**	-	**172.1**
Net book value						
At 31 March 2008	**1.8**	**1.4**	**1,204.9**	**53.3**	**13.6**	**1,275.0**
At 31 March 2007	1 9	1 3	1,211 8	49 3	23 2	1,287 5
Analysis of net book value at 31 March 2008						
Owned	1 8	1 4	1,204 9	52 9	13 6	**1,274.6**
Held under finance lease	-	-	-	0 4	-	**0.4**
	1.8	**1.4**	**1,204.9**	**53.3**	**13.6**	**1,275.0**

6 Fixed asset investments

	Unlisted investments £m
Cost	
At 31 March 2008 and 2007	**0.1**
Amounts written off	
At 31 March 2008 and 2007	-
Net book value	
At 31 March 2008 and 2007	**0.1**

The fixed asset investment represents the Company's shareholding in xoserve Limited The Company's shareholding represents 10% of the issued share capital of xoserve Limited

In addition, the Company owns all of the issued share capital of Wales & West Pension Scheme Trustees Ltd, which is non-trading and comprises 2 shares of £1 each

Consolidated financial statements
The Company has taken the advantage of section 228(1) of the Companies Act 1985 not to produce consolidated financial statements as it is a wholly owned subsidiary of MGN Gas Networks (Senior Finance) Limited

7 Stocks and work in progress

	2008 £m	2007 £m
Raw materials and consumables	**2.6**	2 7

The replacement cost of stocks is not materially different from their carrying value

8 Debtors

	2008 £m	2007 £m
Amounts falling due within one year:		
Trade debtors	**37.3**	34 2
Prepayments and accrued income	**18.9**	8 4
	56.2	42 6

9 Creditors

	Note	2008 £m	2007 £m
(a) Amounts falling due within one year:			
Payments received on account		**28.3**	27 6
Obligations under finance leases	11	**0.1**	0 5
Trade creditors		**13.3**	20 0
Amounts owed to parent undertakings		**422.0**	384 3
Other taxation and social security		**10.5**	8 7
Other creditors		**0.6**	1 7
Capital expenditure contributions		**1.0**	3 0
Accruals and deferred income		**52.5**	39 0
Grants received		**1.5**	0 8
		529.8	485 6
(b) Amounts falling due after more than one year:			
Other loans	10	**960.3**	906 8
Liability for index linked swap contracts		**46.6**	24 5
Obligations under finance leases	11	**-**	0 2
Capital expenditure contributions		**38.3**	24 2
Accruals and deferred income		**1.4**	1 1
		1,046.6	956 8

10 Other loans

	2008 £m	2007 £m
Repayable as follows		
Between two and five years	**960.3**	906 8

The Company's obligations under its loan facility agreements are repayable other than by instalment and are secured by fixed and floating charges over its assets

Floating interest rates on these loans are hedged by interest rate swaps, which range between 1 44% and 1 64% (2007 2 98% and 5 35%) Variable interest rates on loans varied between 0 4% and 1 0% above LIBOR (2007 0 4% to 1 0% above LIBOR)

11 Finance leases

	2008 £m	2007 £m
Amounts due under finance leases are payable as follows		
Within one year	**0.1**	0 5
Between one and two years	**-**	0 2
	0.1	0 7

12 Gross borrowings

	2008 £m	2007 £m
Fınance leases	**0.1**	0 7
Gross value of other loans	**968.0**	918 0
	968.1	918 7

The maturıty profile of the group's gross borrowıngs, excludıng bank overdrafts, but ıncludıng finance leases, was as follows

	2008 £m	2007 £m
In one year or less, or on demand	**0.1**	0 5
In more than one year but not more than two years	**190.0**	0 2
In more than two years but not more than five years	**778.0**	918 0
	968.1	918 7

The dıfference between gross borrowıngs as dısclosed above and net borrowıngs as dısclosed ın notes 10 and 11 reflect the unamortısed element of the debt arrangement fees of £7 7m (2007 £11 2m)

13 Financıal instruments and risk management

(a) Interest rate swaps

The Company has entered ınto ınterest rate swap arrangements ın order to manage the ınterest rate exposure of the Company and not for tradıng or speculatıve purposes

The Company's outstandıng ınterest rate swap arrangement had a notıonal prıncıpal balance of £964m (2007 £964m), wıth termınatıon dates rangıng between November 2023 and November 2039 (2007 31 March 2013), wıth ınterest rates rangıng between 1 44% and 1 64% (2007 2 98% to 5 35%)

As part of the Company's hedgıng strategy, durıng the perıod ended 31 March 2006 the Company acquıred from MGN Gas Networks (Senıor Fınance) Lımıted an ınterest rate swap contract wıth a notıonal value of £924m Thıs contract was recorded ın the accounts of the Company at ıts negatıve faır value on transfer of £50 4m and was offset by an equıvalent reductıon ın the amount that the Company owed MGN Gas Networks (Senıor Fınance) Lımıted through theır intercompany account Durıng the year contracts wıth a notıonal value of £472m have been extended to maturıtıes rangıng between November 2035 and November 2039 The remaınıng £532m of these contracts were cancelled durıng the year and the element of the onerous ınterest rate swap contracts provısıon (£16 5m) relatıng to these cancelled contracts was released to the profit and loss account ın the year (note 16(c)) The remaınıng provısıon wıll be amortısed on a straıght lıne basıs over the extended contract lıves

13 Financial instruments and risk management (continued)

(b) I nterest rate composition of gross borrowings

After taking account of the interest rate swaps entered into by the Company, the fixed and floating interest rate profile of the Company's gross borrowings, including intra-group indebtedness, was

	2008 £m	2007 £m
Fixed rate	**1,244.8**	1,210 3
Floating rate	**89.0**	39 0
Total	**1,333.8**	1,249 3

The gross borrowings with floating interest rates relate to group borrowings

The above analysis includes £365 7m (2007 £330 6m) of intra-group indebtedness to parent undertaking The remaining £56 3m (2007 £53 7m) owed to parent undertakings constitutes the interest accrued on the loan principal Interest was chargeable on these loans at 21% (2007 21%) on the fixed element and LIBOR + 16 4% (2007 LIBOR + 16 4%) on the floating element

(c) Interest rate profile of fixed rate borrowings

After taking account of the interest rate swaps entered into by the Company, the weighted average interest rate profile of the Company's gross borrowings, including intra-group indebtedness, together with the weighted average period for which the rate is fixed was

	Weighted average interest rate		Weighted average period for which rate is fixed	
Currency	**2008 %**	**2007 %**	**2008 Years**	**2007 Years**
Sterling	**8.24**	8 77	**2.2**	3 2

(d) Maturity profile of financial instruments with no interest paid

			Weighted average period until maturity	
	2008 £m	**2007 £m**	**2008 Years**	**2007 Years**
Liability for index-linked swap contracts	**46.6**	24 5	**1.2**	6 1

(e) Borrowing facilities

Undrawn committed borrowing facilities were

	2008 £m	2007 £m
Committed borrowing facilities available	**1,152.0**	1,152 0
Drawn	**(968.0)**	(918 0)
Undrawn facilities as at 31 March 2008 expiring after 31 May 2010	**184.0**	234 0

At the Company's option, £1,120m (2007 £1,120m) of the committed facilities can be extended to 31 May 2015 (2007 31 May 2015)

13 Financial instruments and risk management (continued)

(f) Fair values of financial instruments

In the table below, the fair value of short term borrowings, current asset investments, cash at bank and in hand and bank loans approximates to book values due to the short maturity of these instruments

The fair values of long term instruments have been determined by reference to prices available from the financial markets on which these borrowings are traded The fair values fundamentally represent the change in anticipated future interest rates, to the dates of maturity of the borrowings, between the date on which those long term borrowings were raised and the year end This increased liability will only materialise if the Company ceases trading and future anticipated interest rates remain at year end levels

	Book value £m	Fair value £m
Primary financial instruments held or issued to finance the Company's operations:		
Short term borrowings	**(0.1)**	(0 1)
Long term borrowings	**(968.0)**	(968 0)
Cash at bank and in hand	**27.3**	27 3
	(940.8)	(940 8)
Derivative financial instruments held to manage the interest rate profile and matched by primary financial instruments:		
Interest rate swaps	**(66.3)**	(165 7)
	(1,007.1)	(1,106 5)

The fair value of derivative financial instruments matched to primary financial instruments relates to long term borrowings with a book value of £960 3m (2007 £906 8m) which have been included within the primary financial instruments issued to finance the Company's operations at a fair value of £968m (2007 £918m), which is the redemption value of those borrowings The difference between gross borrowings as disclosed above and net borrowings as disclosed in notes 10 and 11 reflect the unamortised element of the debt arrangement fees of £7 7m (2007 £11 2m)

(g) Losses on derivative financial instruments

The fair value of losses on derivative financial instruments is not recognised in the financial statements These instruments are held to manage the Company's interest rate exposures and the resultant fixed interest charges are made in the accounting periods to which they relate The table below analyses the composition of the fair value losses (note 13(f)) Of these losses £119 1m (2007 £32 4m) are entirely notional and would only materialise if the Company were to cease trading

	Total losses £m
At 1 April 2007	**(32.4)**
Movement in fair value	**(133.3)**
At 31 March 2008	**(165.7)**
Of which:	
Losses not expected to be included in 2008/09 or later years	**(119.1)**
	(119.1)

The difference between the total losses and the losses not expected to be included in 2008/9 or later years is the amount accrued in the financial statements of £46 6m (note 9(b)) in respect of liability for index linked swap contracts

14 Capital commitments

	2008 £m	2007 £m
Contracted for but not provided in the financial statements	5.3	2 9

In order to meet regulatory and service standards, the Company has longer term capital expenditure obligations within the regulated gas distribution business, which include investments to meet shortfalls in performance and condition, and to provide for new demands and growth

The recent regulatory review period ended on 31 March 2008 The determination for the five year regulatory period ended 31 March 2013 has been agreed and includes capital and replacement investment of £275 3m for capital work and £368 5m for replacement work (in 2005/6 prices)

15 Leasing commitments

	Land and buildings		Others	
	2008 £m	2007 £m	2008 £m	2007 £m
At 31 March 2008 there were revenue commitments, in the ordinary course of business in the next year to the payment of rentals on non cancellable operating leases expiring				
Within one year	0.5	-	0.2	0 6
Between two and five years	0.3	0 6	0.6	0 4
After five years	0.6	0 6	-	-
	1.4	1 2	0.8	1 0

16 Provisions for liabilities and charges

	Note	2008 £m	2007 £m
Claims provision	(a)	**3.0**	1 6
Environmental and demolition provisions	(b)	**21.9**	20 4
Onerous interest rate swap contracts provision	(c)	**19.7**	40 0
Onerous contracts provision	(d)	**1.2**	0 4
Wayleaves provision	(e)	**2.8**	2 3
Other provisions	(f)	-	0 6
Deferred taxation	(g)	-	-
		48.6	65 3

(a) Claims provisions

	2008 £m	2007 £m
At 1 April	**1.6**	2 0
Increase in provision	**1.9**	-
Utilised in the year	**(0.5)**	(0 4)
At 31 March	**3.0**	1 6

The claims provision is the estimate of liabilities in respect of past events incurred by the business On the transfer of the business to the Company on 1 May 2005, these liabilities were established at a fair value of £2m In accordance with insurance industry practice, these estimates were based on experience from previous years and there was, therefore, no identifiable payment date During the year the Company reassessed the provision based on claims experience since 1 May 2005

(b) Environmental and demolition provisions

	2008 £m	2007 £m
At 1 April	**20.4**	18 6
Unwinding of discount (note 3b)	**0.9**	1 9
Charge for the year	**0.8**	-
Utilised in the year	**(0.2)**	(0 1)
At 31 March	**21.9**	20 4

The environmental provision represents the estimated environmental restoration and remediation costs relating to a number of sites owned and managed by the Company The provision has been discounted to its estimated net present value The anticipated timing of the cashflows for statutory decontamination cannot be predicted with certainty, but it is expected to be incurred over the period 2008 to 2057

(c) Onerous interest rate swap contracts provision

	2008 £m	2007 £m
At 1 April	**40.0**	45 9
Released in the year	**(16.5)**	-
Utilised in the year	**(3.8)**	(5 9)
At 31 March	**19.7**	40 0

As part of the Company's hedging strategy, during the period ended 31 March 2006 the Company acquired from MGN Gas Networks (Senior Finance) Limited an interest rate swap contract with a notional value of £924m This contract was recorded in the accounts of the Company at its negative fair value on transfer of £50 4m and was offset by an equivalent reduction in the amount that the Company owed MGN Gas Networks (Senior Finance) Limited through their intercompany account During the year contracts with a notional value of £472m have been extended to maturities ranging between November 2035 and November 2039 The remaining £532m of these contracts were cancelled during the year and the element of the onerous interest rate swap contracts provision (£16 5m) relating to these cancelled contracts was released to the profit and loss account in the year The remaining provision will be amortised on a straight line basis over the extended contract lives

16 Provisions for liabilities and charges (continued)

(d) Onerous contracts provision

	2008 £m	2007 £m
At 1 April	**0.4**	0 6
Charge for the year	**1.1**	-
Utilised in the year	**(0.3)**	(0 2)
At 31 March	**1.2**	0 4

The onerous contracts provision represents the expected costs incurred in relation to vacant properties owned by the Company and a loss making contract The provision was reassessed in the year and is expected to be utilised in the two years ended 31 March 2010

(e) Wayleaves provisions

	2008 £m	2007 £m
At 1 April	**2.3**	2 7
Unwinding of discount (note 3(b))	**0.6**	-
Utilised in the year	**(0.1)**	(0 4)
At 31 March	**2.8**	2 3

The wayleaves provision is provided to cover the costs associated with rectifying gas distribution assets which are the subject of ineffective easements or wayleaves The provision is expected to be utilised over the period until 2020

(f) Other provisions

	2008 £m	2007 £m
At 1 April	**0.6**	0 6
Released in the year	**(0.6)**	-
At 31 March	**-**	0 6

Other provisions provide for a potential liability in respect of contracts which have repayment clauses in the event that certain future thresholds are achieved The Company no longer consider that a liability will crystallise under the contract and accordingly the provision has been released

(g) Deferred taxation

The movement on deferred tax is as follows

	2008 £m	2007 £m
At start of year	-	-
Profit and loss account	-	-
At end of year	-	-
Deferred tax provided is made up as follows		
Accelerated capital allowances	-	-
Other timing differences	-	-
Tax losses carried forward	-	-
	-	-

A deferred tax asset has not been recognised in respect of accelerated capital allowances and total tax losses with a tax value of £48 6m (2007 £30 8m) as there is insufficient evidence that the asset will be recoverable

17 Called up share capital

	2008 £	2007 £
Authorised		
Ordinary shares of £1 each	**30,675,000**	30,675,000
Allotted, called up and fully paid		
Ordinary shares of £1 each	**30,675,000**	30,675,000

18 Reserves ~ Profit and loss account

	£m
At 1 April 2007	**(212.9)**
Loss retained for the year	**(106.1)**
Actuarial loss on pension scheme	**(5.7)**
Movement on deferred tax relating to pension scheme	**-**
At 31 March 2008	**(324.7)**
Pension liability recorded in reserves	**25.2**
Profit and loss reserves excluding pension liability	**(299.5)**

19 Net Cash inflow from operating activities

	2008 £m	2007 £m
Continuing operations		
Operating profit/(loss)	**17.5**	(0 5)
Depreciation of tangible fixed assets	**67.4**	53 2
Amortisation of capital contributions	**(1.8)**	(0 5)
Profit on disposal of fixed assets	**(0.3)**	(0 3)
Net decrease in stocks	**0.1**	0 1
Net increase in debtors	**(1.9)**	(2 5)
Net increase in creditors	**8.8**	10 3
Difference between pension charge and cash contributions	**(5.5)**	2 3
Movements in provisions for liabilities and charges	**2.3**	0 8
Net cash inflow from operating activities	**86.6**	62 9

20 Analysis of changes in financing in the year

	Share capital		Long term loans & finance lease obligations	
	2008 £m	2007 £m	2008 £m	2007 £m
At 1 April	**30.7**	30 7	**907.5**	866 4
Long term loans	-	-	**50.0**	39 0
Amortised debt arrangement fees	-	-	**3.5**	3 5
Finance lease repayments	-	-	**(0.6)**	(1 4)
At 31 March	**30.7**	30 7	**960.4**	907 5

21 Analysis of changes in cash and cash equivalents in the year

	2008 £m	2007 £m
At 1 April	26.9	29 9
Net cash inflow/(outflow)	0.4	(3 0)
At 31 March	27.3	26 9

22 Analysis of cash and cash equivalents

	2008 £m	2007 £m	2008 Change in year £m	2007 Change in year £m
Cash at bank and in hand	27.3	26 9	0.4	(3 0)

23 Reconciliation of net cash flow to increase in net debt

	2008 £m	2007 £m
(Decrease)/increase in cash as per cash flow statement	0.4	(3 0)
Increase in loans	(50.0)	(39 0)
Amortisation of debt arrangement fees	(3.5)	(3 5)
Finance lease repayments	0.6	1 4
Increase in net debt	(52.5)	(44 1)
At 1 April	(880.6)	(836 5)
At 31 March	(933.1)	(880 6)

24 Directors' and officers' loans and transactions

No loans or credit transactions with any directors, officers or connected persons subsisted during the year or were outstanding at the end of the year

25 Pension scheme

The Company operates one pension scheme which has defined contribution and defined benefit sections

Defined benefit section

The Company operates a defined benefit pension scheme, the Wales & West Utilities Pension Scheme ("the Scheme") The Scheme funds are administered by trustees and are independent of the Company's finances Contributions are paid to the Scheme in accordance with the Schedule of Contributions agreed between the Trustees and the Company

A full actuarial valuation as at 31 March 2006 was completed The calculations carried out to produce the results of this valuation were updated to the accounting date by an independent qualified actuary in accordance with FRS17 As required by FRS17, the value of the defined benefit liabilities has been measured using the projected unit method

The key FRS17 assumptions used for the Scheme are set out below, along with the fair value of assets, a breakdown of the assets into the main asset classes, the present value of the FRS17 liabilities and the deficit of assets below the FRS17 liabilities (which equals the gross pension liability)

Assumptions	**2008**	**2007**	**2006**
Price inflation	**3.6% pa**	3 1% pa	2 9% pa
Discount rate	**6.1% pa**	5 2% pa	5 0% pa
Pension increases (LPI)	**3.6% pa**	3 1% pa	2 9% pa
Salary growth	**4.85% pa**	4 35% pa	3 9% pa

On the basis of the assumptions used for life expectancy, a male pensioner currently aged 60 would be expected to live for a further 26 years (2007 26 years) Allowance is made for future improvements in life expectancy For example, a male member who is aged 60 in the year 2027 would be expected to live for a further 27 years (2007 27 years)

Asset distribution and expected return

	2008		**2007**		**2006**	
	Expected return % pa	**Fair value £m**	**Expected return % pa**	**Fair value £m**	**Expected return % pa**	**Fair value £m**
Equities	**8.5% pa**	**135.8**	8 8	144 3	8 4	133 8
Bonds & cash	**4.5% pa**	**44.1**	4 5	23 7	4 2	17 3
Property	**6.5% pa**	**14.1**	6 5	15 8	6 3	13 7
Total		**194.0**		183 8		164 8

25 Pension scheme (continued)

Balance sheet

	2008 £m	2007 £m	2006 £m
Total fair value of assets	**194.0**	183 8	164 8
FRS17 value of liabilities	**(224.2)**	(218 1)	(180 1)
Gross pension liability	**(30.2)**	(34 3)	(15 3)

The scheme is represented on the balance sheet at 31 March 2008 as a liability under FRS17 which amounts to £30 2m (2007 £34 3m)

Over the year to 31 March 2008, contributions by the Company of £20 9m (2007 £5 4m) were made in respect of members of the defined benefit section In addition, £0 7m (2007 £0 7m) has been set aside by the Company outside of the Scheme during the year in order to meet the Scheme's expenses It has been agreed that future ongoing employer contributions will be at a rate of 36 7% (2007 20 7%) of pensionable salary plus an allowance for expenses In addition, the Company has agreed to pay deficit recovery contributions of £5 2m pa until 31 March 2013 plus £1 7m pa for the period from 1 April 2010 to 31 March 2013

The post retirement deficit under FRS17 moved over the year as follows

	2008 £m	2007 £m
Post retirement deficit at 1 April	**(34.3)**	(15 3)
Current service cost (employee and employer)	**(10.8)**	(9 4)
Contributions (employee and employer)	**22.5**	7 1
Curtailment loss	**(5.8)**	-
Other net finance income	**3.9**	3 9
Actuarial loss	**(5.7)**	(20 6)
Post retirement deficit at end of year	**(30.2)**	(34 3)

The following amounts have been included within operating profit under FRS17 for the defined benefit section

	2008 £m	2007 £m
Current service cost (employer's part only)	**9.9**	8 5
Curtailment cost	**5.8**	-
Total operating charge	**15.7**	8 5

The following amounts have been included as net finance income under FRS17

	2008 £m	2007 £m
Expected return on pension scheme assets	**15.6**	13 1
Interest on post retirement liabilities	**(11.7)**	(9 2)
Net return to credit to finance income	**3.9**	3 9

The scheme is now closed to new entrants and, under the method used to calculate pension costs in accordance with FRS17, the cost as a percentage of covered pensionable payroll will tend to increase as the average age of the membership increases

25 Pension scheme (continued)

The followmg amounts have been recognised within the statement of total recognised gains and losses ("STRGL") under FRS17

	Note	2008 £m	2007 £m
Actual return less expected return on scheme assets	(a)	(25.8)	-
Experience gains and (losses) arising on scheme's liabilities	(b)	-	(2 1)
Gain or (loss) due to changes in assumptions underlying the FRS17 value of scheme liabilities		20.1	(18 5)
Actuarial loss recognised in the STRGL	(c)	(5.7)	(20 6)

The history of experience gains and losses is

Note		2008	2007	2006
(a)	Actual return less expected return on scheme assets	£(25.8)m	-	£21 9m
	Percentage of scheme's assets	(13)%	0%	13%
(b)	Experience gains and (losses) arising on scheme's liabilities	-	£(2 1)m	-
	Percentage of the FRS17 value of the scheme's liabilities	-	(1)%	-
(c)	Total amount recognised in the STRGL	£(5.7)m	£(20 6)m	£1 1m
	Percentage of the FRS17 value of the scheme's liabilities	(3)%	9%	1%

Defined contribution scheme

The Company also operates a defined contribution scheme for staff

The employer paid a further £0 6m (2007 £0 8m) during the accounting period in respect of defined contribution members

26 Parent company

The immediate parent company is MGN Gas Networks (Senior Finance) Ltd and the ultimate parent company is MGN Gas Networks (UK) Ltd Copies of the annual accounts of MGN Gas Network (UK) Ltd may be obtained from The Company Secretary, MGN Gas Networks (UK) Ltd, Wales & West House, Spooner Close, Celtic Springs, Coedkernew, Newport, NP10 8FZ

27 Related party transactions

(a) Gas purchases
Under its licence condition, the Company is required to purchase gas to cover certain "own use" activities including own consumption in operating the gas distribution network and shrinkage due to estimated losses from the network

The Company has contracted with Macquarie Bank Limited ("MBL") to purchase the gas it requires to fulfil these commitments The contract was awarded to MBL after it won a competitive tender process These transactions are carried out on an arms length basis and the prices charged are compared to available quoted gas purchases prices to ensure they are competitive The cost of purchasing this gas amounted to £7 1m (2007 £7 1m) in respect of the year

(b) xoserve Limited
The Company owns 10% (2007, 10%) of the issued share capital of xoserve Limited ("xoserve") xoserve is owned jointly by the UK Gas Distribution companies and National Grid group as owner of the gas transmission business in the UK

xoserve provides gas throughput (meter reading) and billing information to the Company which is used by the Company in setting its regulated gas distribution charges to gas transporters The cost to the Company of xoserve providing these services was £3 5m (2007 £3 3m) in respect of the year, of which £0 3m (2007 £0 1m) was charged to capital

(c) Hedging Transactions
As discussed in Note 13 (a), the Company's outstanding interest rate swap arrangement had a notional principal balance of £964m (2007 £964m), with a termination dates ranging between November 2023 and November 2039 (2007 31 March 2013), with real interest rates ranging between 1 44% and 1 64% (2007 2 98% to 5 35%)

The swap arrangements are split between seven counterparty banks, one of which is Macquarie Bank Limited ("MBL") There were £118m of outstanding swap transactions with MBL at 31 March 2008 (2007 £241m) The swap arrangements are on an arms length basis

MBL were engaged as advisors to the Group in the restructure of its interest rate swap arrangements The cost to the Company of MBL providing these services was £0 7m (2007 £nil)

(d) Corona Energy Retail Ltd group
The Company provided gas transportation services to the three companies in the Corona Energy Retail Ltd ("Corona") group Corona is owned by Macquarie Bank Limited These services are provided on normal commercial terms in common with all other gas shippers operating in the Company's geographic region The income to the Company in respect of these services to the Corona Energy Retail group was £5 8m (2007 £4 1m)